United States

Estate and Income Taxation of Non-Resident Aliens

Materials

by

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Prologue: Why Is Estate Planning For Non-U.S. Persons Important?

1. U.S. Estate Tax on Non-U.S. Estates can be very onerous:

a. Current highest U.S. federal estate tax rate is 40% (essentially, a U.S. taxable estate is currently taxed at a 40% rate for every dollar that such taxable estate exceeds $5,490,000 (2017, indexed for inflation for years thereafter).

b. Exemption from U.S. federal estate tax for an estate of a non-U.S. decedent is limited to $60,000. So the U.S. federal estate tax on a U.S. taxable estate of just $1,000,000 would exceed $300,000.

c. No credit is allowed under U.S. federal estate tax law for estate or inheritance taxes paid to a non-U.S. jurisdiction on U.S. property unless provided for under a transfer tax treaty between the U.S. and such foreign jurisdiction.

d. To obtain the marital deduction for a transfer on death to a non-U.S. citizen spouse, a QDOT trust must be established, but, it should be noted that most civil law jurisdictions do not honor—and may even discriminate against—trusts (for example, the 2011 Amended Finance Act of the Republic of France).

e. Unless a treaty allows otherwise, the charitable estate tax deduction is limited to transfers to U.S. qualifying organizations (that is, pursuant to IRC § 2106(a)(2), no charitable estate tax deduction is available for a gift to a corporate charity unless it is a U.S. domestic charity, and no charitable estate tax deduction is available for a gift to a charitable trust unless the gift is to be used only within the U.S.). Furthermore, if the gifted property was not required to be included in decedent's U.S. gross estate, then no charitable estate tax deduction is available even though such property was bequeathed to a U.S. charity (see IRC § 2106(a)(2)(D)).

f. The disclosure of a decedent's worldwide assets is required in order to claim deductions for estate administration expenses allocable to U.S. property and charitable transfers (see IRC § 2106(b)).

g. The disclosure of a decedent's worldwide assets is also required in order to deduct any portion of the debts of a non-U.S. decedent unless they are non-recourse.

h. State estate tax or inheritance taxes may also apply, especially with regard to real estate that a non-resident non-citizen of the United States ("NRNC") owns directly. IRC § 2106(a)(4) allows "state death taxes" generally to be deductible against U.S. federal estate tax on the U.S. estate of a deceased NRNC in the same proportion that the property subject to state death taxes bears to the total value of U.S. property subject to U.S. federal estate tax.

2. Risk of Paying Unnecessary Taxes

Without proper planning, non-U.S. clients could pay estate tax unnecessarily to United States, but have no—or insufficient—estate/inheritance tax in their own jurisdiction against which they could claim credits for the U.S. estate tax paid.

a. Some Countries have no Estate/Inheritance or Death-Related Tax:

- Argentina (outside of Buenos Aires): http://www.globalpropertyguide.com/Latin-America/Argentina/Inheritance
- Australia: http://www.globalpropertyguide.com/Pacific/Australia/Inheritance
- Austria: http://www.stepjournal.org/jurisdictions/jurisdictional_summaries/austria/4_taxation.aspx
- China: http://www.globalpropertyguide.com/Asia/China/Inheritance [1]
- India: http://www.globalpropertyguide.com/Asia/India/Inheritance [2]
- Mexico: http://www.solutionsabroad.com/en/legal/legal-category/mexican-will-and-estate-planning.html
- New Zealand: http://www.dol.govt.nz/immigration/knowledgebase/item/3307
- Russia: http://www.worldwide-tax.com/russia/rus_econonews.asp
- Sweden: http://www.dollarsandsense.org/archives/2005/0905miller.html

b. Some Countries may, depending on circumstances, have generally lower rates of Estate/Inheritance Tax, especially for the inheritance of property by immediate descendants.

- Belgium: Highest tax rate for descendants and ascendants appears to be is 30% in the Brussels region: http://www.cfe-eutax.org/taxation/inheritance-tax/belgium
- Brazil: Highest rate is 8%.

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[1] See Galligan, Kolodny & Wang, “Modern Inheritance Develops in China,” New York Law Journal (February 17, 2007), http://www.phillipsnizer.com/publications/articles/ModernInheritChina2-07_art.cfm

[2] See Galligan and Schiller, “U.S.A. Tax Effects of Hindu Undivided Families,” Legal Era (October 2010), http://phillipsnizer.com/pdf/Article-LegalEra-HinduUndividedProperty-10-2010.pdf

http://www.globalpropertyguide.com/Latin-America/Brazil/Inheritance

- Germany: Highest tax rate for descendants and ascendants appears to be 30%: http://www.barandt.com/e_new_german_inheritance_tax_law.html

- Italy: The highest tax rate appears to be 8%. http://www.globalpropertyguide.com/Europe/Italy/Inheritance

- Netherlands: The highest rate for spouses and children appears to be 20%. http://blog.clvn.nl/blog/2010/09/are-you-subject-to-dutch-inheritance-tax.html

- Switzerland: Highest rate in Canton of Geneva is 26%. Highest rates in many other canons are lower. http://www.globalpropertyguide.com/Europe/Switzerland/Inheritance

3. Non-tax problems that impact on U.S. estate tax planning.

a. Who is the "Fiduciary" or Non-U.S. "Executor? Many jurisdictions have very attenuated concept, if any, of "executor" to which U.S. assets can be transferred without U.S. probate.

- Application of NY EPTL § 13-3.4 ("Payment or delivery of property to foreign fiduciaries") is uncertain.

- Transfer agents will often require U.S. federal "transfer certificate" and are generally unaware of the IRS "safe harbor" provisions under Treas. Reg. § 20.6325-1(b)(3).

b. Problems in making foreign testamentary documents operate on U.S. Property.[3]

- Lack of familiarity by U.S. courts with notarial and other forms of civil Wills

- Difficulty in coordinating U.S. and non-U.S. property concepts:[4]

  ™ Universal heir vs. residuary estate

  ™ Usufruct vs. life estate

  ™ Lack of trust concept

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[3] See Galligan, "Buying USA: Ways of Minimizing U.S. Transfer Taxes on U.S. Property Interests of Non-U.S. Persons," STEP USA (June 2007), http://www.phillipsnizer.com/pdf/Article-STEPJournalUSASupplementIssue3Galligan.pdf. (This article is also attached to this Outline as Exhibit B).

[4] See Galligan, "International Estate Planning for U.S. Citizens: An Integrated Approach," 36 Estate Planning No. 10, 11 (October 2009), http://www.phillipsnizer.com/publications/articles/IntlEstatePlanIntegApproach_art.cfm.

™ Holographic wills vs. Witnessed Wills

™ Notarial Wills vs. Witnessed Wills

c. Possible Application of Non-U.S. Law

Subjecting assets to U.S. administration could subject intangible assets to forced heirship rules (because of U.S. choice of law rules), even though most U.S. jurisdictions do not themselves adopt compulsory inheritance rules.

4. U.S. Federal Taxes To Which Non-U.S. Persons can Be Subject

- Federal Estate Tax
- Federal Gift Tax
- Federal Generation-Skipping Transfer Taxes
- Federal Income and Gains Taxes

Be aware of matching or "tag along" state or municipal taxes in all these cases.

The Scope of the Federal Estate Tax

The estate tax under Subchapter A of Chapter 11 of Subtitle B only applies to the transfer of the estate of U.S. citizen decedents and U.S. "resident" decedents.

The estate tax on the transfer of estates of "nonresidents" who are not U.S. citizens is imposed by Subchapter B of Chapter 11 of Subtitle B and only applies to "that part of [their] gross estate (determined as provided in Section 2031) which at the time of their death is situated in the United States."

The Scope of the Federal Gift Tax

The gift tax imposed by Chapter 12 of Subtitle B applies to the transfer of property by gift "by any individual resident or nonresident" with an exception for transfers of "intangible property by a nonresident not a citizen of the United States" (other than certain expatriates).

The Scope of the Generation-Skipping Transfer Tax

The GST Tax imposed by Chapter 13 of Chapter B applies to all "generation-skipping transfers," including (i) direct transfers, (ii) certain trust distributions and (iii) certain trust terminations. However, by regulation § 26.2663-2(b), the GST Tax only applies to direct transfers or transfers in trust by a nonresident not a citizen of the United States that were subject in the first place to U.S. estate or gift tax.

The Scope of the Federal Income Tax

The income tax imposed by Subchapter A of Chapter 1 of Subtitle A is imposed on all married individuals, heads of household, surviving spouses, unmarried individuals, estates and trusts, and corporations.

"Nonresident Aliens"

Need to distinguish "non-resident aliens" for income tax purposes from "non-resident aliens" for transfer tax purposes:

<u>Income Tax NRAs</u> are generally individuals who are not lawfully admitted to the U.S. for permanent residency and do not meet the "substantial presence" test for U.S. income tax residence under IRC § 7701(b)(3).[5]

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[5] A foreign national is considered to be resident in the United States for U.S. federal income tax purposes (and thereby would be subject to U.S. income tax on his worldwide income) if he meets either of the "lawful permanent residence" test or the "substantial presence" test. [IRC § 7701(b)(1)(A)].

Under the lawful permanent residence test, the foreign national is considered resident in the U.S. from the day he enters the U.S. with a "green card" until the day that his "green card" status is revoked by the immigration authorities or that such status has been judicially determined to have lapsed. During the period that the foreign national maintains his "green card" status, he is considered to be resident in the U.S. for income tax purposes even if he is living at the time outside the U.S.

Under the "substantial presence" test, the foreign national is considered resident in the U.S. for U.S. income tax purposes if (1) he is present in the U.S. for at least 31 days during the current calendar year, and (2) he is present in the U.S. for a weighted average of at least 183 days over a three-year look-back period which includes the current calendar year and the two preceding calendar years (in determining the weighted average, all days present in the U.S. during the current calendar year are counted, but only one-third of the days present in the preceding year and one-sixth of the days present in the next preceding year are counted). Furthermore, in applying the "substantial presence" test, the foreign national must include any day on which he was present any time at all within the U.S.

<u>Example One</u>

Non-Resident

	2015	**2016**	**2017**	
Days	121	121	121	
Calculation	20 $^1/_{16}$	40 $^1/_3$	121 =	181 $^1/_2$

<u>Example Two</u>

Resident

	2015	**2016**	**2017**	
Days	122	122	122	
Calculation	20 $^1/_3$	40 $^2/_3$	122 =	183

IRC § 872(a) limits the "gross income" of "nonresident alien individuals" (including estates and trusts pursuant to IRC § 641(b)) to only

- Gross income derived from sources within the United States that is not "ECI" income (IRC § 871(a)).[6] This is generally taxed at a flat 30% rate (or lower treaty rate) without the allowance of deductions. But note that certain categories of U.S. investment income such as interest on qualifying U.S. bank accounts and so-called "portfolio debt" as described in IRC § 871(h) is effectively exempt from tax under IRC § 871(a) provided that such interest does not constitute ECI.

- Gross income that is "ECI" – that is, "effectively connected with the conduct of a trade or business within the United States" (IRC § 871(b)). This is taxed at graduated rates on a net basis.

a. IRC § 882(b) applies the identical rules to "foreign corporations"

b. Generally, no capital gains tax on disposition of U.S. intangible property and tangible personal property not ECI, owned by persons who are not U.S. citizens or U.S. income tax residents. [But see IRC § 871(a)(2) where such capital gains are subject to U.S. income taxation in the case where the NRA is present in the U.S. for at least 183 days during the year (e.g., a foreign exchange student in the U.S. under an "F" or "M" visa).]

c. But capital gains tax is imposed on dispositions of U.S. real property interests (both direct interests in U.S. real property and U.S. corporations with substantial holdings of U.S. real property) owned by persons who are neither U.S. citizens nor U.S. income tax residents. See IRC § 897 ("FIRPTA").

Note that there are several exceptions to the "substantial presence test" that allow certain categories of foreign nationals to avoid being treated as resident aliens even though their presence in the U.S. would satisfy the three-year look-back rule (for example, foreign government employees holding "A" visas, and, in certain instances, foreign exchange students holding "F" or "M" visas).

Further note that IRC § 7701(b)(3)(B) provides for an exception to the "substantial presence" test in the case of a foreign national who has 183 or more "deemed days" under the three-year look-back rule, but whose actual days present in the United States during the current calendar year is less than 183. The foreign national qualifies for this exception only if (1) he has a "tax home" in a foreign country for the current calendar year; (2) he has a "closer connection" with the same foreign country than he has with the U.S. for the current calendar year; (3) he does not have an application for "adjustment of status" pending at any time during the current calendar year, nor has he taken any actions to apply for a "green card"; and (4) he timely files with his U.S. income tax return, IRS Form 8840 or its equivalent disclosing to the IRS that that he qualifies for the IRC § 7701(b)(3)(B) exception.

[6] Two types of U.S.-source income are taxable under this category: 1) "fixed or determinable annual or periodical gains, profits, and income" (commonly referred to as "FDAP income") taxed under IRC § 871(a)(1) and 2) U.S.-source capital gains, taxable under IRC § 871(a)(2), if the NRA was present in the U.S. for at least 183 days during the year of sale. (The HIRE Act of 2010 enacted the tax provisions of the so-called "Foreign Account Tax Compliance Act" ("FATCA"), which include provisions imposing U.S. withholding tax on certain "dividend equivalent" amounts paid or credited to non-U.S. persons on or after September 14, 2010.).

Discussion

Key Planning Issues:

I. What is the Citizenship of the Client?

To be treated as a non-U.S. person (and thus not subject to universal U.S. federal transfer taxes) a client cannot be a U.S. citizen.

Establishing U.S. Citizenship

A. Birth in the U.S. unless to non-U.S. diplomats.

B. Birth abroad to two U.S. citizen parents as long as one parent resided for a certain period in the U.S. or possession.

C. Birth abroad to a U.S. citizen and non-U.S. citizen depends on length of U.S. residence of U.S. citizen parent and age when such residence took place.

D. Birth of U.S. citizen to U.S. father out of wedlock requires some U.S. residence by father and legitimization or acknowledgement of paternity prior to age 18 of child.

E. Birth of U.S. citizen to mother out of wedlock requires mother to be physically present in U.S. or possession continuously 12 months before birth of child.

F. Naturalization.

G. Naturalization by parents if occurs before age 18.

H. Child Citizenship Act of 2000: at least one U.S. citizen parent and child admitted to U.S.A. as legal permanent resident if conditions are satisfied before age 18.

Helpful Reference:

See "Tables of Transmission Requirements Over Time for Citizenship for Certain Individuals Born Abroad," Appendix B to Ira Kurzban, Immigration Law Sourcebook (Fifteenth Edition, 2016, AILA).

Note: Citizens Resident in U.S. Possessions

U.S. citizen who acquired U.S. citizenship solely by reason of

1. being a citizen of a U.S. possession or birth or

2. residence within a U.S. possession is considered a "non-resident not a citizen of the United States" for purposes of all taxes under Subtitle B (gift, estate, GST).

II. What is Domicile of the Client?

Note: To be treated as a non-U.S. person (and therefore subject to U.S. transfer taxes only on transfers of U.S. situs property), the client cannot be domiciled in the United States.

Meaning of "United States" To be a U.S. resident for U.S. transfer tax purposes, domicile must be established in one of the States of the United States or the District of Columbia.

A. Definition of Treas. Reg. § 20.0-1

"A person acquires a domicile in a place by living there, for even a brief period of time, with no definite present intention of later removing therefrom"

1. Need intention to remain indefinitely
2. Intention to change not effective unless implemented

Thus, the definition of "domicile" clearly carries within it two necessary elements, those being (1) physical presence in a country and (2) intent to remain there indefinitely. Since physical presence is usually easy to determine, the essential element in determining domicile is whether taxpayer had intent to remain there indefinitely. The courts look to a variety of factors in gauging the intention of an individual to live in the U.S. with no definite present intention of relocating. It should be noted that while the case law provides helpful guidance, there is no bright line test in determining intent as every case has its own unique particulars and the issue of intent must be decided in the light of the facts peculiar to each case.

A typical list of factors that are considered in determining domicile include—but are not limited to—the duration of stay in the U.S. and in other countries, the relative nature, size, and cost of the individual's residences, the location of the individual's family, the location of the individual's personal possessions, the location of the individual's business interests, the place where the individual has stronger communal ties and maintains memberships in religious, professional, and social organizations, the location of bank accounts, declarations of residence or intent made in visa applications, wills, etc., and the individual's motivations for being in the United States and being abroad

B. Notable Cases on Domicile

1. <u>Estate of Nienhuys</u> (47 T.C. 1149 (1952)) – Netherlands citizen declares to U.S. Immigration Authorities intent to reside permanently in U.S.A. and receives a "green card," but is still found to be domiciled in The Netherlands (Tax Court found the particular facts convincing that the Netherlands citizen with a U.S. green card was not living in the U.S. by choice, but rather because Germany had invaded the Netherlands and that

he always hoped to return to The Netherlands if and when circumstances improved. He lived in a modest apartment in the U.S. though he could afford a higher-end residence which he continued to own in The Netherlands. His declaration on his visa applications were made while Germany was occupying the Netherlands).

2. Estate of Khan (T.C. Memo 1998-22 (1998)) – Pakistani citizen who lived his entire life in Pakistan (except for approximately seven years when he was residing in the U.S. and tending to his business and property interests which were more significant than the interests he held in Pakistan) and who died in Pakistan more than four years after he was last present in the U.S. is still found to be domiciled in the U.S. Tax Court found that, when decedent came to the U.S. on his last "tour of duty," he entered on a permanent resident visa, obtained a "green card" and social security number, and intended to stay to tend to his more significant business interests and that, when he left for Pakistan two years later (and never to return), he did so not to abandon his "U.S. domicile" but rather only to visit his family and to resolve some business matters. The court found that decedent's effort to obtain a U.S. re-entry permit at around the time of his departure to Pakistan was indicative that decedent did not intend to change his domicile from the U.S.

3. Estate of Jack (54 Fed. Cl. 590 (2002)) – Canadian citizen present in the U.S. and teaching at a California university on a temporary non-immigrant visa (in particular, a TN Temporary Professional visa) could be found to have established U.S. domicile for U.S. federal estate tax purposes despite the fact that an intent to remain permanently in the U.S. would violate the terms of his non-immigrant visa. Federal Claims Court ruled that the IRS should not be precluded from showing that decedent's domiciliary intent changed or was other than what he previously represented to immigration officials in his visa application. (But see, Carlson v. Reed, 249 F.3d 876 (9th Cir. 2001)).

An important "take away" from these cases and others[7] is that estate and tax planners must pay attention to practically every aspect of their clients' personal and professional lives in advising them as to how a U.S. court might rule on domicile.

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[7] Some other notable decisions include Estate of Paquette, T.C.Memo 1983-571 (1983); Estate of Fokker, 10 T.C. 1225 (1948); Elkins v. Moreno, 435 U.S. 647 (1978) (employees of international organization present in the U.S. on non-immigrant "G-4 visa" could still be found to be domiciled in the U.S. for U.S. federal estate tax purposes); Estate of Bloch-Sulzberger, 6 T.C.M. 1201 (1947).

C. Special Cases Where the Question of Domicile May Be Ambiguous

1. Persons who are considered domiciliaries of their country of nationality even after they have established domiciliary in different country (tax treaties).

   For example, under the U.S.-U.K. estate and gift tax treaty, a U.K. national (and domiciliary) who moves to the U.S. may still be deemed to maintain his domicile in the U.K. for a period of time after the move, at least if the U.K., under its own internal rules, considers the U.K. national to be a U.K. domiciliary for any period after his departure from the U.K. (See Article 4(2)(b) of such treaty, which provides that if such U.K. national had not been resident in the U.S. for Federal income tax purposes in 7 or more of the 10 taxable years ending with the year in which the death or transfer occurs, he may be deemed to be domiciled in the U.K. at that time.).

2. Persons who have "green cards" but who do not have an intention to remain indefinitely in the U.S.

3. Persons who have conditional "green cards"

   a. Marriage to U.S. citizen

      A foreign national's permanent residence is conditional if it is based on a marriage that was less than 2-years old on the day such foreign national was given permanent residence. The foreign national could apply to remove the conditions on permanent residence if such foreign national is still married to the same U.S. citizen (or permanent resident) after 2 years.

   b. Foreign National present in the U.S. under an EB-5 visa.

      An EB-5 visa is a method of obtaining a green card for certain foreign nationals who invest money in the U.S. If the foreign national investor's visa application is approved, the investor and his dependents will be granted conditional permanent residence valid for two years Within 90 days before the conditional "green card" is set to expire, the investor must provide evidence showing that the full required investment has been made and that, as a result, a certain minimum number of jobs in the U.S. have been created or preserved or will be created within a reasonable time. If the investment fails, the foreign national must leave the U.S.

4. Former U.S. Citizens and Long-Term U.S. Residents who Expatriated Prior to June 17, 2008, the date that the new 2008 Expatriation Rules became effective under the HEART Act:

a) Persons who renounced U.S. citizenship or gave up "green card," are deemed to have a tax-avoidance reason for doing so (10 year application).

b) Persons who spend substantial time in U.S.A. (10 year application)

Note: Do not confuse U.S. domicile with U.S. income tax residence:

1. A "green card" holder is subject to U.S. worldwide income tax regardless of plans to stay indefinitely or to leave after future occurrence

2. Application of "days test" is mechanical except for narrow exception under IRC § 7701(b)(3)(B)

III. What Property Does A Client Own And What Is Its Nature?

A. What Are The Forms Of Ownership That Count?

1. Distinction Between Legal Title and Beneficial Ownership

Title: Trust, Stiftung, Corporate Nominee…

Beneficial: Trust Beneficiary, Foundation Distributee, Beneficial Owner of Assets Held in Corporate Name …

Treas. Reg. § 20.2013-5(a)

> ". . . the term "property" means any beneficial interest in property, including a general power of appointment . . . over property. Thus, the term does not include an interest in property consisting merely of a bare legal title . . ."

Special Cases:

- Application of IRC § 2104(a): Stock "owned and held" by a nonresident noncitizen of the U.S. ("NRNC") subject to U.S. estate tax only if issued by U.S. corporation. However, stock of a foreign corporation is <u>not</u> includible in the U.S. estate of a NRNC, regardless of whether the stock certificates are actually located within the U.S. [See Treas. Reg. § 20.2105-1(f)].

  <u>See</u> <u>Estate of Charania v. Shulman</u>, 608 F.3d 67 (1st Cir. 2010), <u>aff'g in part</u>, 133 T.C. 122 (2009) (stock of Citigroup held subject to U.S. estate tax, undiminished by alleged community property share of surviving spouse).

  American Depositary Receipts ("ADRs"), although normally issued and sold by U.S. banks are considered to have situs outside the U.S. because they substantively are treated as shares in foreign corporations. [See PLR 200243031].

Investments in U.S. real property owned by Canadian mutual funds that were a part of NRNC decedent's RRSP held not includible in NRNC decedent's U.S. estate because the Canadian mutual funds were determined to have foreign situs as they were properly classified as corporations incorporated outside the United States. [See CCA 201003013].

* Risk of non-U.S. corporations holding U.S. assets being considered nominees for their shareholders: See <u>Fillman v. U.S.</u>, 355 F.2d 632 (Cl. Ct. 1966).

The situs rule for stock of foreign corporations has resulted in the use of foreign holding corporations as a major estate planning tool to prevent assets of a NRNC, which would otherwise have U.S. situs if held directly, from being subject to U.S. federal estate tax. The <u>Fillman</u> case strongly cautions planners that more is required than simply placing U.S. situs assets in a foreign corporation. At a minimum, the corporation should be in good standing under local law and corporate formalities should be followed.

* Risk that, in certain circumstances, a transfer of U.S. stock to a foreign holding company may cause the foreign holding company ("inverted" or "surrogate foreign corporation") to be treated under, IRC § 7874(b), as a U.S. corporation for all tax purposes under the Internal Revenue Code, notwithstanding IRC § 7701(a)(4).

- Application of IRC § 2104(b): Trusts funded with U.S. property or holding U.S. property upon death of NRNC settlor in which NRNC settlor has retained right of enjoyment or incidents of control treated as de facto nominee for U.S. assets held by trust or attributable to U.S. property with which trust was funded upon death of NRNC settlor. [See TAM 9507044 (February 17, 1995) (trust funded with U.S. property).].

* Risk that non-U.S. partnerships and non-U.S. LLCs holding U.S. assets, if otherwise qualifying as non-U.S. assets, may be considered nominees for their partners holding U.S. assets: See <u>Matter of Strangi</u>, TC Memo 2003-145 (2003), aff'd 417 F.3d 468 (5th Cir. 2005)

B. What Property Does the Client Share with Others?

1. Matrimonial Property Regimes

   a. Separate Property

   b. Community Property as to Marital Property

   c. Community Property as to All Property of the Spouses

Special Cases:

1. Germany: Separate Property with "Community of Surplus."[8]

2. New Zealand: Matrimonial Property Law.

3. United States: Spousal Right of Election.

Note: New York has adopted the New York Uniform Disposition of Community Property Rights at Death Act. NY EPTL §§ 6-6.1 through 6-6.7.

2. Forms of Common Law Joint Ownership (Tenants by Entirety, Joint Tenants with Survivorship) as distinguished from Tenants in Common.

U.S. Citizen Spouses: Property assumed owned 50/50 for Federal Estate tax purposes.

Non-U.S. Citizen Spouses:

One or Two Non-citizen Spouses:	Property subject to estate tax based on contribution.
Gifts of real property:	Contribution rule for gift tax purposes is applied on distribution of proceeds of sale.
Gifts of intangible property:	Contribution rule for gift tax purposes is applied when joint interest is established.[9]

See Estate of Charania v. Shulman, 608 F.3d 67, 73 (1st Cir. 2010), aff'g in part, 133 T.C. 122 (2009) – The estate of the deceased U.K. NRNC,

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[8] "Zugewinngemeinschaft."

[9] See Dina Kapur Sanna, "Unexpected Gift Tax From Joint Accounts With Foreign Spouse," Estate Planning Journal (December 2011).

who owned stock of Citigroup directly, argued that one-half of the stock was owned by surviving spouse as community property, but couple did not take steps under Belgian law to declare a community property regime and U.K. precedent applicable to NRNC did not consider change of matrimonial domicile from separate property jurisdiction (Uganda) to Belgium sufficient to effect change from separate property to community property.

Note: Non-Citizen Spouses

- Enlarged annual exclusion for gifts of "present interests" to non-U.S. citizen spouses: The exclusion is indexed for inflation and is currently at $139,000 for 2012.
- No QDOT Trust is available for lifetime gifts to non-U.S. citizen spouses.
- If either or both spouses are NRNCs, no "gift-splitting" (attributing the gift of one spouse to both spouses to maximize utilization of gift tax exclusions and exemptions) not permitted. IRC § 2513(a)(1).

C. What Property Owned by Client Might be Subject to Claims of Others?

1. "Clawback Provisions" under Forced Heirship Statutes

Spain:	No statutory limit on look-back to transfers made during lifetime (but limitations may be supplied by courts)
Switzerland:	Look-back for most part, limited to five years
France:	Surviving spouse may withdraw gifts made to predeceased spouse

2. Testamentary Substitutes Under Spousal Right of Election

a. Unlimited look-back (subject to enactment dates) for transfers into trust with retained interest. NY EPTL § 5-1.1-A(b)(1)(F)

b. One year look-back for all direct gift transfers. NY EPTL § 5-1.1-A(b)(1)(B)

Note: Spousal right of election in New York is not available to spouse of non-New York domiciliary decedent unless decedent made an election to have disposition of New York property governed by New York law under EPTL § 3-5.1(h).

D. What Property of Client Is Subject to Creditors’ Claims?

1. In many civil law jurisdictions, heirs (absent express election to contrary) take decedent’s property, subject to unlimited liability for decedent’s debts.

2. In New York, generally, claims of creditors of decedent limited to estate assets but an heir can also be liable for debts to the extent of property received from estate for debts not satisfied from assets subject to administration (NY EPTL § 12-1.1).

IV. Where Is Client’s Property Located?

A. For Purposes of Determining Applicable Inheritance Law

1. Civil Law Tradition Generally:

    a. No Distinction Between Real and Intangible Property (No “Scission”)

    b. Applicable Law is Based on Citizenship

    c. Is the applicable law the “Whole Law” (or “Substantive Law” only)?

        Germany (yes)

        Italy (probably yes)

        Spain (no – but there may be different views)

    d. “Renvoi” from the Country of Citizenship increasingly applied

2. Common Law:

    a. Distinction between real property and intangible property (“scission”)

    b. Real property governed by law where property is located

    c. Intangible Property governed by law of domicile or owner (individual or trustee); “mobilia sequuntur personam" ("moveable assets follow the person").

Mixed Situations

- France

  - Recognizes Scission.
  - Immoveable property follows law of situs.
  - Moveable property follows law of domicile.

- Switzerland
  - Generally, does not recognize scission
  - Habitual residence rather citizenship is key factor

B. **For Purposes of New York EPTL § 3-5.1(h) and EPTL § 7-1.10**

- Real property and tangible property located in New York

Bank and Brokerage Accounts with New York branches of banks and brokerage houses. See Hutchinson v. Ross, 262 N.Y. 381 (1933) (Quebec domiciliaries) (“Tangible chattels and securities”) – not following rule of “mobilia sequuntur personam.” Wyatt v. Fulrath, 38 Misc. 2d 1012 (1963) (Spanish domiciliaries) (joint bank accounts).

- Entities organized by New York and physical documents maintained here

C. **For purposes of N.Y. EPTL § 7-1.10**

“Whenever a person, not domiciled in this state, creates a trust which provides that it shall be governed by the laws of this state, such provision shall be given effect in determining the validity, effect and interpretation of the disposition in such trust of:

1) Any trust property situated in this state at the time the trust is created

2) Personal property, wherever situated, if the trustee of the trust is a person residing, incorporated or authorized to do business in this State or a national bank having an office in this State.”

In re Tabbaghi’s Estate, 167 Misc. 156 (1938) (France) (validity of trust)

D. **For purposes of N.Y. EPTL § 3-5.1(h)**

“Whenever a testator, not domiciled in this state at the time of death, provides in his will that he elects to have the disposition of his property situated in this state governed by the laws of this state, the intrinsic validity, including the testator’s general capacity, effect, interpretation, revocation or alteration of any such disposition is determined by the local law of this state."

See Estate of Renard, 56 N.Y.2d 973 (1982) (bank and brokerage accounts)

E. **For Purposes of U.S. Federal Gift Tax and Gift-Related GST Tax**

1. Real Property Located in U.S. treated as U.S. situs. [See Treas. Reg. § 25.2511-3(b)].

   * Possibility of gifts of non-U.S. cash by NRNC intended to facilitate purchase of U.S. real property could be characterized as real property itself, under IRS "step transaction" theory. [See De Goldschmidt-Rothschild v. Commissioner, 168 F.2d 975 (2d Cir. 1948); Davies v. Commissioner, 40 T.C. 525 (1963).].

2. Tangible Personal Property located in U.S. treated as U.S. situs. [See Treas. Reg. § 25.2511-3(b)].

   * Vexed issue about funds in U.S. bank deposit accounts for U.S. gift tax purposes

   A gift by an NRA by means of a check drawn against his U.S. bank account or a wire transfer to a donee's U.S. account may be treated as a gift of currency, in which case, it would likely be treated by the IRS as a gift of tangible personal property located in the U.S. [See Treas. Reg. § 25.2511-3(b)(4)(iv); PLR 7737063; GCM 36860 (Sept. 24, 1976); Rev. Rul. 55-143].

   An NRA who desires to make a cash gift and avoid IRS potentially characterizing it as a taxable gift should not issue a check on a U.S. bank account or wire funds from a U.S. bank account, but rather should wire funds from his offshore account to offshore accounts held by the U.S. donees or should withdraw cash from a U.S. account and give out the cash to the U.S. donees outside the U.S.

3. Intangible Personal Property with U.S. connections treated as foreign situs. For example, a gift of U.S. corporate stock by a non-resident alien is exempt from gift tax even if the stock certificate is physically located in the U.S. [See IRC § 2501(a)(2)].

F. **For Purposes of U.S. Federal Estate Tax and Estate-Related GST Tax**

1. Real Property Located in the United States has U.S. situs. [See Treas. Reg. § 20.2104-1(a)(1)].

   Note: Remember that "real property" under common law has a narrower definition than "immovable property" under civil law

2. Tangible Personal Property

Tangible Personal Property that is not being used or loaned for exhibition or related purposes and that is located in the United States has U.S. situs. [See Treas. Reg. § 20.2104-1(a)(2)].

Note: Currency is treated as tangible personal property for estate tax purposes. [See Rev. Rul. 55-143].

3. Shares of Stock of U.S. Corporations

Shares of stock issued by a U.S. "domestic" corporation (regardless of location of certificates) have U.S. situs. [See IRC § 2104(a); Treas. Reg § 20.2104-1(a)(5)].

a. IRC § 2104(a) refers to shares "owned and held" by an NRA.

b. Treas. Reg. § 20.2104-1(a)(5) omits the reference to "owned and held."

c. Note: A transfer tax treaty may override the Code's inclusionary rule as to stock of U.S. corporations. For example, generally, under the "modern" U.S. estate tax treaties (for example, treaties with the United Kingdom, France, Germany, and The Netherlands), the U.S.'s treaty partner has the exclusive right to tax stock in U.S. corporations where the decedent is determined to be a domiciliary of such treaty partner.[10]

d. For an estate of a NRNC decedent who died after 2004 and before 2012, if such NRNC decedent had owned stock of a U.S. mutual fund or "regulated investment company" (i.e., "RIC"), only the proportion of the fund invested in U.S. situs assets are subject to U.S. estate tax. IRC § 2105(d). The purpose of this rule was to provide an exemption to the estates of foreign persons who invest in certain assets through a RIC to the same extent that those assets would not be subject to the estate tax if held directly. However, for NRNC decedents dying in 2012 and thereafter, the exception of IRC § 2105(d) is no longer applicable and shares in RICs (i.e., domestic mutual funds) are fully includible in the U.S. estate of a NRNC by virtue of IRC § 2104(a).

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[10] See Galligan, "Making Sense of Four US Estate Tax Treaties: US-Netherlands, US-Germany, US-France, US-UK," NYSBA International Law Practicum (Spring, 2004), http://phillipsnizer.com/pdf/Article-MG-4TransAtlanticTaxTreaties-Spring04.pdf . See also Glenn G. Fox, "U.S. Estate Planning for Nonresident Aliens from Treaty Countries: A Comparison of Germany, Austria, France and the United Kingdom," http://www.alston.com/files/Publication/8e33adc5-36ec-44c6-b393-15a5eb07710e/Presentation/PublicationAttachment/f41b680f-0675-48ce-9790-9ca67f1ae75d/FoxBNA%20Article%20on%20Estate%20and%20Treaty%20Planning%20for%20NRAs.DOC

4. Debt Obligations of U.S. Persons

Debt obligations of a U.S. person, the U.S. or a political subdivision if not treated as "outside the U.S." by IRC § 2105 have U.S. situs.

a. In the case of NRNCs who <u>are not</u> U.S. income tax residents, debt obligations that have U.S. situs include:

   (i) Portfolio debt issued on or prior to July 18, 1984

   (ii) Debt issued by companies in which the NRNC held 10% or more of the voting power (corporation) or capital or profits interest (partnership) [IRC § 871(h)(3)(B)].

   (iii) Obligations issued by state and local municipalities[11]

   (iv) Obligations subject to profitability or similar contingencies [IRC § 871(h)(4)(A)].

   (v) Bearer bonds described in IRC § 163(f)(2)(B) and are issued on or after March 19, 2012.

b. In the case of NRNCs who <u>are not</u> U.S. income tax residents, the following debt obligations have foreign situs:

   Debt obligations that are portfolio debt obligations (except for those enumerated in (i) through (v) above) are generally foreign situs, even if issued by a U.S. person, if issued after July 18, 1984. [IRC § 2105(b)(3)]. This generally applies to debt obligations if any interest thereon would be eligible for the exemption from U.S. income tax under IRC § 871(h)(1) were such interest received by the NRA decedent at the time of his death, without regard to whether the U.S. issuer has received a statement (that satisfies the requirements of IRC § 871(h)(5)) that the beneficial owner of the obligation is not a U.S. person. The term "portfolio interest" also includes interest that is paid on a non-registered obligation (like a bearer bond) that was issued before March 19, 2012 and that is described in IRC § 163(f)(2)(B). Debt obligations considered as having foreign situs, for decedents dying after August 5, 1997, also include short-term obligations (OID) with maturity dates of 183 days or less as long as any interest thereon is not effectively connected with a U.S. trade or business. [IRC § 2105(b)(4)].

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[11] Due to the technicality that the IRS § 871(h) income tax exemption only applies if interest is exempt only by virtue of IRC § 871 (but "query" whether such income is exempt under general principles of U.S. tax law).

c. In the case of NRNCs who <u>are</u> U.S. income tax residents, all U.S. debt obligations have U.S. situs – because U.S. income tax residents are not eligible for the exemptions described in IRC § 871(h).[12]

5. Certain Deposits

a. A NRNC's deposit with a domestic bank is not considered to have a U.S. situs as long as the deposit is not effectively connected with a trade or business conducted by the NRNC within the U.S. [IRC § 2105(b)(1)]. Additionally, a deposit in an offshore branch of a U.S. domestic bank is also deemed to have a foreign situs. [IRC § 2105(b)(2)].

Any conventional bank deposit (for example, funds in checking and savings accounts and in certificate of deposits) are considered under the above rule of IRC § 2105(b) to have foreign situs.

In PLR 200842013, the IRS ruled that annuity proceeds due a NRNC decedent, but still held by the insurance companies as of the decedent's death, were <u>not</u> deemed to have U.S. situs pursuant to IRC § 2105(b)(1) and therefore were excluded from NRNC's gross estate under IRC § 2103.

b. The following deposits have U.S. situs:

Special deposits held by U.S. banks in a custodial capacity that are not commingled with other assets of the bank. [See Rev. Rul. 69-596].

Deposits with brokerage houses

Deposits with U.S. branches of foreign corporations that are engaged in the commercial banking business (and do not fit within the portfolio interest exclusion)

6. Other Intangible Property

"Intangible Personal Property, the written evidence of which is not treated as being the property itself, if it is issued by or enforceable against a U.S. resident or a domestic corporation or governmental entity." Treas. Reg. § 20.2104-1(a)(4)

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[12] Further details on inclusion and exclusion of debt instruments as well as on many other topics related to U.S. estate tax planning for NRNCs may be found in Michael A. Heimos, 837-3rd Tax Management Inc., Non-Citizens – Estate, Gift and Generation-Skipping Taxation.

a. "Property the written evidence of which is treated as being the property itself" was thought to include bonds for the payment of money (see Treas. Reg. § 20.2104-1(a)(3))

b. "U.S. resident" is presumably defined as U.S. domiciliary.[13]

c. Possible Application:

   (i) Partnerships

   (ii) Limited Liability Companies

   (iii) Intellectual Property Rights

   (iv) License rights

Special Note on Partnerships

(a) Often thought of as intangible personal property

(b) General partners generally have rights to terminate partnership and therefore may be seen as owning shares of the underlying partnership property

See Sanchez v. Bowers, 70 F.2d 715 (2nd Cir. 1934)

(c) Rev. Rul. 55-701 (situs is where partnership does business) should not be applicable

   a. Decided under superseded U.S.-UK Estate Tax Convention

   b. Treas. Reg. § 20.2104-1 was amended in 1973 and 1974 and did not adopt this rule

(d) "Look-through" rule of Sanchez v. Bowers, 70 F.2d 715 (2d Cir. 1934) generally applied only to general partnerships or perhaps interests of general partners in limited partnerships.

(e) Case for applying the rule of Blodgett v. Silberman, 277 U.S. 1 (1928) uses the common law 'domicile of decedent' rule for situs of intangible property. How strong is this position?

   (i) Depends on contention that Treas. Reg. § 20.2104-1(a)(4) was not intended to apply due to the language therein suggesting that it has limited applicability

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[13] Treas. Reg. § 20.2104-1(a)(7) refers by contrast, to U.S. person as defined in IRC § 7701(a)(30) for U.S. income tax purposes

or

(ii) Depends on contention that Treas. Reg. § 20.2104-1(a)(4) is "ultra vires" because it addresses issues not explicitly addressed by IRC § 2104.

Important Principle:

> "State law creates legal interests and rights. The federal revenue acts designate what interests and rights, so created, shall be taxed."

Morgan v. Commissioner, 309 U.S. 78, 80 (1940)

Therefore, only express departures from state law concepts by Federal tax law regarding situs of property should be valid.

Special Note on Limited Liability Companies

(a) In the absence of an election to the contrary, a U.S. LLC is treated for all U.S. tax purposes as a partnership if it has two or more members. Treas. Reg. § 301-7701-3(b).

(b) In the absence of an election to the contrary, a single-member LLC is disregarded.

(c) In the absence of an election to the contrary, a non-U.S. LLC is treated for U.S. tax purposes as a partnership if it has two or more members and one member does not have limited liability.

(d) LLCs generally did not exist under U.S. law in 1955 – therefore even better argument that Rev. Rul. 55-701 does not apply.

(e) Sanchez v. Bowers should not apply when there are no "general partners."

(f) LLCs were still rare in early 1970's when Treas. Reg. § 2104-1(a)(4) was last amended.

(g) Argument in favor of applying the Blodgett rule attributing situs to domicile of owner of LLC interest may be stronger than with a partnership interest.

7. Trusts

"Look-through" Rules for Trusts

(i) U.S. property transferred "in trust or otherwise" in which decedent retained an interest (under IRC §§ 2035 through 2038) at the time of death (IRC § 2104(b)).

(ii) Property (even non-U.S. property) held "in trust or otherwise" that originated from U.S. property transferred to the trust by the decedent (IRC § 2104(b)).

(iii) Non-U.S. situs share of property held by a U.S. regulated investment company ("RIC") (2005-2011) is eligible for exclusion.

Cases and Rulings

Swann v. Commissioner, 247 F.2d 144 (2d Cir. 1957): Stiftung treated as a U.S. trust with retained interest despite provision of U.S.-Switzerland income tax treaty treating Stiftung as corporation.

TAM 9507044 – Trust created in 1923 with U.S. assets subject to U.S. estate tax even though assets in trust when grantor died in 1991 had non-U.S. situs.

But see CCA 201020009 (payment of gift tax within 3 years of NRNC decedent's death considered made under IRC § 2035(b) is not a transfer within the meaning of IRC §§ 2035 to 2038; thus such gift tax paid is not property deemed situated in the U.S. under IRC § 2104(b)).

V. What Planning Entities Work Best for Client?[14]

A. Corporations

1. Consider Treas. Reg. § 20.2105-1(f)

> "Shares of stock issued by a corporation which is not a domestic corporation, regardless of the location of the certificates" are treated as outside the U.S.

2. Consider whether the stock of foreign corporation must be "owned and held" by non-U.S. shareholder.

3. Avoid having the corporation be treated as a nominee for foreign shareholder. See Fillman v. U.S., 355 F.2d 632 (Ct. Cl. 1966).

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[14] For an overview, see the discussions in Robert F. Hudson, Jr., "The U.S. Tax Effects of Choice of Entities for Foreign Investment in U.S. Real Estate and Businesses and the Taxation of Dispositions of U.S. Partnership Interests," http://www.iirusa.com/upload/wysiwyg/U1986/IIR_U1986_Hudson.pdf; Richard Lehmann, "United States Taxation of Foreign Investors," http://www.lehmantaxlaw.com/unitedstatestaxation.html; Cassell, Karlin, McCaffrey & Streng, "U.S. Estate Tax Planning for Nonresident Aliens Who Own Partnership Interests," http://www.bryancave.com/files/News/051c9e1d-a8a6-4d16-84d2-8aee4140f817/Presentation/NewsAttachment/051ab3f8-07ff-4ab5-8540-8c6edfe6e2c5/RCassell%20article.pdf.

4. Consider U.S. income tax consequences if foreign corporation holds U.S. assets directly.

    a. Corporate capital gains tax rates on sale of U.S. real property (FIRPTA)

    b. Possible branch profits tax on U.S. business activities; not applicable at least in cases where sole asset of foreign corporation is U.S. real estate that does not generate income, or where income is reinvested in the real estate, as long as corporation is liquidated soon after sale of real estate.

       If foreign corporation is in a treaty jurisdiction, treaty may provide branch profits tax relief.

    c. Possible loss of tax treaty benefits if foreign corporation is in a tax-haven jurisdiction.

5. Consider U.S. income tax consequences if direct owner of U.S. assets is U.S. corporation owned by foreign corporation.

    a. Corporate capital gains tax rates on sale of all U.S. assets

    b. No branch profits tax

    c. U.S. withholding tax on payment of dividends to foreign corporate parent, subject to reduced treaty rates depending on residence of foreign corporation; no such withholding tax if earnings are reinvested and paid out to foreign corporate parent upon liquidation of U.S. corporation after payment of U.S. capital gains tax on sale of assets it holds.

6. Consider non-U.S. income tax consequences, especially if corporation is not organized in client’s primary tax jurisdiction.

7. Consider U.S. tax consequences if corporate stock is later owned by U.S. persons:

    (a) Loss of step-up in basis for assets held by corporation

    (b) Treatment of foreign corporation if treated as CFC or PFIC

B. Partnerships and LLCs Qualifying as Partnerships[15]

1. U.S. Partnership still may be vulnerable to U.S. estate tax inclusion (Risk)
2. Foreign Partnerships may be vulnerable to U.S. estate tax inclusion if engaged in U.S. business activities (Risk)
3. Share of U.S. Capital Gains taxed at Individual Rates (Advantage)
4. Availability of IRC § 754 election to "step-up" internal basis of partner's share of underlying assets to match the post-death external basis. (Advantage)
5. No U.S. NRA withholding tax; tax treaty benefits may be more accessible; and no branch profits tax (Advantage).
6. If primary taxing jurisdiction accepts partnership treatment, may be more acceptable to that jurisdiction (Advantage).
7. Would not be treated as CFC or PFIC if passes to U.S. owners (Advantage).

C. Consider Combination of U.S. LLC and Foreign Corporation

a. LLC organized in U.S. jurisdiction could establish U.S. situs for non-tax purposes but be disregarded for U.S. tax purposes if owned by sole foreign person.

b. Corporation not owned abroad but owned by LLC would still be treated as owner of assets for U.S. tax proposes.

c. Possible approach to combining benefits of U.S. tax planning for non-U.S. person, with protection from foreign property law issues under EPTL § 3.5-1(h) and/or EPTL § 7-1.10. (See Exhibit A).[16]

U.S. assets owned by non-U.S. corporation

Non-U.S. corporation owned by single-member N.Y. LLC

Single member of LLC is either:

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[15] Note that, under Rev. Proc. 2012-7, the IRS will not issue rulings as to whether a partnership interest is intangible property for purposes of gifts by NRNCs and therefore will not be subject to U.S. gift tax, pursuant to IRC § 2501(a)(2).

[16] For further discussion of these provisions of New York law, see Galligan, "Forced Heirship in the United States of America," in these materials for the Eighth Annual NYSBA-STEP International Estate Planning Institute.

… Non-U.S. individual with Will directing application of N.Y. law to N.Y. property

or

N.Y. trust directing that N.Y. law govern the trust.

D. **Insurance**

Wrapping U.S. property in insurance vehicles that qualify as insurance for U.S. tax purposes and where the insurance is on the life of the owner of the policy.

Life insurance on the owner of the policy as source of funding for assets that have to be owned directly by non-U.S. person (no U.S. estate planning need for irrevocable life insurance trust because of life insurance exclusion under IRC § 2105(a)).

VI. What To Do When The Client Has Already Acquired U.S. Property In Client's Own Name?

A. **Gifts**

Lifetime gifts of intangible U.S. property, including stock of U.S. corporations, U.S. partnership interests, notes, intellectual property rights, claims are all exempt from U.S. gift tax.

Lifetime gifts of real and tangible property located in the United States do not provide very much relief since there is no lifetime gift tax exemption for NRNCs. [IRC § 2505(a)]. Annual exclusion is available (currently $13,000 per donee) but this is not likely to be of much avail. Gift tax exclusion of educational and medical expenses may be helpful when cash gifts are made from U.S. accounts, granted some uncertainties about the characterization of funds from such accounts as tangible or intangible property, but hardly help with problems involving U.S. real estate or U.S. tangible property that a NRNC may own directly. [IRC §§ 2503(b) & (e)].

B. Exchanges of U.S. assets for stock or membership interest in a non-U.S. entity (Generally, no U.S. capital gains tax on sale or exchange of U.S. intangible property and tangible property by person who is neither U.S. citizen nor U.S. income tax resident; see also IRC § 351(a) and IRC § 721(a) non-recognition rules).

Caution: Plan to avoid potential application of IRC § 7874(b) to cause the foreign corporation to be treated as a domestic corporation for U.S. tax purposes.

IRC § 7874(b) applies where stock in a U.S. corporation is (or the U.S. assets of a U.S. corporation are) transferred to a foreign holding company whereby (1) the

U.S. corporation becomes a subsidiary of such foreign holding company (or substantially all of the U.S. assets of the U.S. corporation are now held by the foreign holding company); (2) the former shareholders of the U.S. corporation hold at least 80% of the foreign holding company's stock by vote or value after the transfer; and (3) the foreign holding company and its "expanded affiliated group" do not have substantial business activities in the foreign country where the foreign holding company is organized.

C. U.S. Real Property Interests ("USRPI")

Capital Contribution of USRPI to foreign corporation subject to tax. IRC § 897(j)

Exchange of direct interest in real property for stock of foreign corporation will trigger tax. IRC § 897(e)(1) and Temp. Reg. § 1.897-6T(b)(3).

Possibility under certain circumstances of deferral of tax on exchange of interest in U.S. Real Property Holding Corporation ("USRPHC") for stock of a foreign corporation. Temp Reg. § 1.897-6T(b)(1).

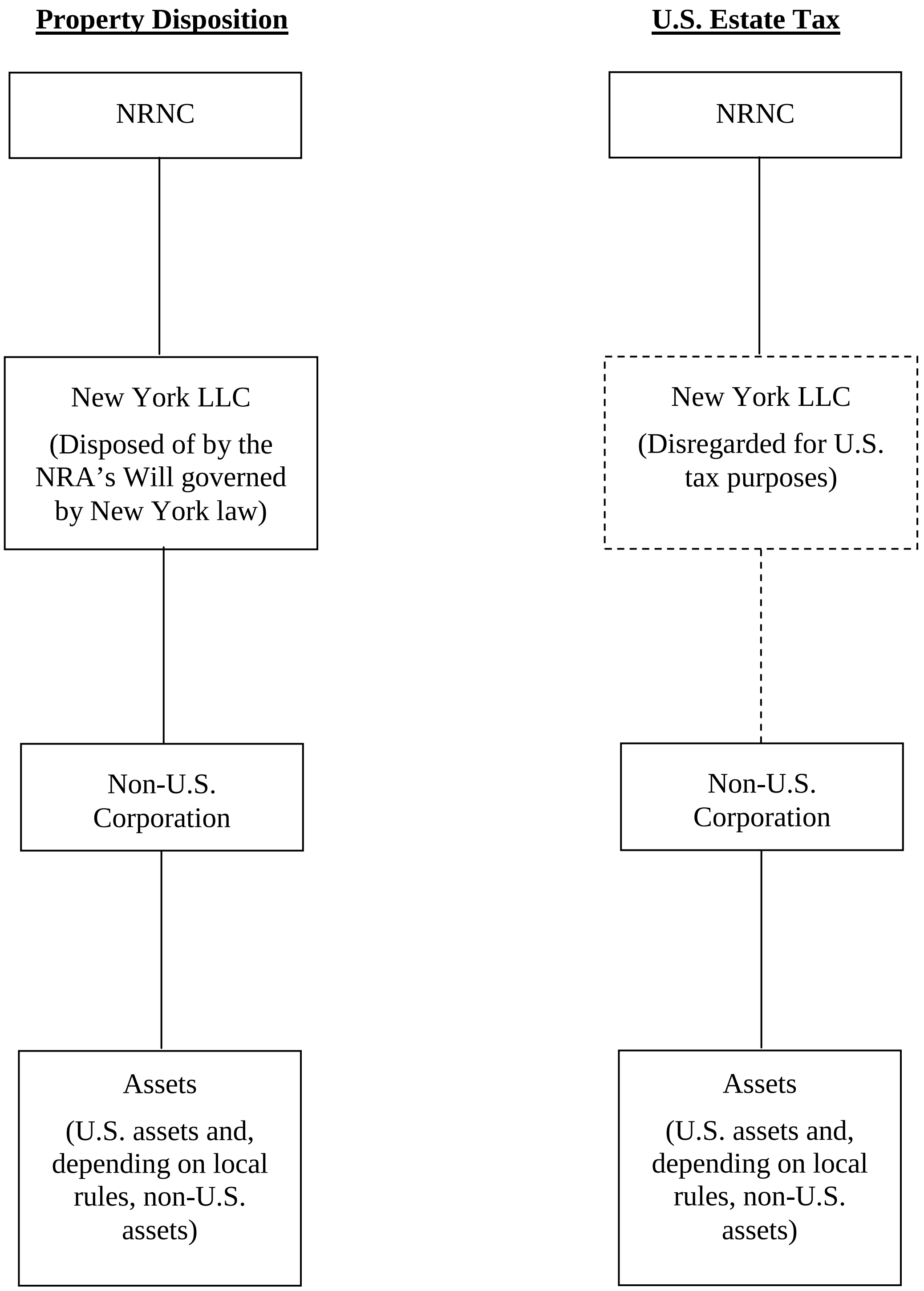
Exchange of direct interest in U.S. real property or an interest in a USRPHC eligible for nonrecognition under IRC § 721 subject to potential recognition under IRC § 897(e) but Temp. Reg. § 1.897-6T(a)(3) provides:

> "For example, the exchange of a U.S. real property interest for an interest in a partnership will receive non-recognition treatment . . . only to the extent that a disposition of the partnership interest will be subject to U.S. taxation by reason of the operation of Section 897(g)."

Another approach to Real Property: encumber real property with non-recourse debt.

Exhibit A

U.S. NRNC Estate Planning Under New York EPTL Section 3-5.1(h)



United States

Estate and Income Taxation of Non-Resident Aliens

Materials

by

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Prologue: Why Is Estate Planning For Non-U.S. Persons Important?

1. U.S. Estate Tax on Non-U.S. Estates can be very onerous:

   a. Current highest U.S. federal estate tax rate is 40% (essentially, a U.S. taxable estate is currently taxed at a 40% rate for every dollar that such taxable estate exceeds $5,490,000 (2017, indexed for inflation for years thereafter).

   b. Exemption from U.S. federal estate tax for an estate of a non-U.S. decedent is limited to $60,000. So the U.S. federal estate tax on U.S. taxable estate of just $1,000,000 would exceed $300,000.

   c. No credit is allowed under U.S. federal estate tax law for estate or inheritance taxes paid to a non-U.S. jurisdiction on U.S. property unless provided for under a transfer tax treaty between the U.S. and such foreign jurisdiction.

   d. To obtain the marital deduction for a transfer at death to a non-U.S. citizen spouse, a QDOT trust must be established, but, it should be noted that most civil law jurisdictions do not honor—and may even discriminate against—trusts (for example, the 2011 Amended Finance Act of the Republic of France).

   e. Unless a treaty allows otherwise, the charitable estate tax deduction is limited to transfers to U.S. qualifying organizations (that is, pursuant to IRC § 2106(a)(2), no charitable estate tax deduction is available for a gift to a corporate charity unless it is a U.S. domestic charity, and no charitable estate tax deduction is available for a gift to a charitable trust unless the gift is to be used only within the U.S.). Furthermore, if the gifted property was not required to be included in decedent's U.S. gross estate, then no charitable estate tax deduction is available even though such property was bequeathed to a U.S. charity (see IRC § 2106(a)(2)(D)).

   f. The disclosure of a decedent's worldwide assets is required in order to claim deductions for estate administration expenses allocable to U.S. property and charitable transfers (see IRC § 2106(b)).

   g. The disclosure of a decedent's worldwide assets is also required in order to deduct any portion of the debts of a non-U.S. decedent unless they are non-recourse.

   h. State estate tax or inheritance taxes may also apply, especially with regard to real estate that a non-resident non-citizen of the United States ("NRNC") owns directly. IRC § 2106(a)(4) allows "state death taxes" generally to be deductible against U.S. federal estate tax on the U.S. estate of a deceased NRNC in the same proportion that the property subject to state death taxes bears to the total value of U.S. property subject to U.S. federal estate tax.

2. Risk of Paying Unnecessary Taxes

Without proper planning, non-U.S. clients could pay estate tax unnecessarily to United States, but have no—or insufficient—estate/inheritance tax in their own jurisdiction against which they could claim credits for the U.S. estate tax paid.

a. Some Countries have no Estate/Inheritance or Death-Related Tax:

- Argentina (outside of Buenos Aires): http://www.globalpropertyguide.com/Latin-America/Argentina/Inheritance
- Australia: http://www.globalpropertyguide.com/Pacific/Australia/Inheritance
- Austria: http://www.stepjournal.org/jurisdictions/jurisdictional_summaries/austria/4_taxation.aspx
- China: http://www.globalpropertyguide.com/Asia/China/Inheritance[1]
- India: http://www.globalpropertyguide.com/Asia/India/Inheritance[2]
- Mexico: http://www.solutionsabroad.com/en/legal/legal-category/mexican-will-and-estate-planning.html
- New Zealand http://www.dol.govt.nz/immigration/knowledgebase/item/3307
- Russia: http://www.worldwidetax.com/russia/rus_econonews.asp
- Sweden: http://www.dollarsandsense.org/archives/2005/0905miller.html

b. Some Countries may, depending on circumstances, have generally lower rates of Estate/Inheritance Tax, especially for the inheritance of property by immediate descendants.

- Belgium: Highest tax rate for descendants and ascendants appears to be is 30% in the Brussels region: http://www.cfe-eutax.org/taxation/inheritance-tax/belgium
- Brazil: Highest rate is 8%.

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[1] See Galligan, Kolodny & Wang, "Modern Inheritance Develops in China," New York Law Journal (February 17, 2007), http://www.phillipsnizer.com/publications/articles/ModernInheritChina2-07_art.cfm

[2] See Galligan and Schiller, "U.S.A. Tax Effects of Hindu Undivided Families," Legal Era (October 2010), http://phillipsnizer.com/pdf/Article-LegalEraHinduUndividedProperty-10-2010.pdf

http://www.globalpropertyguide.com/Latin-America/Brazil/Inheritance

- Germany: Highest tax rate for descendants and ascendants appears to be 30%: http://www.barandt.com/e_new_german_inheritance_tax_law.html

- Italy: The highest tax rate appears to be 8%. http://www.globalpropertyguide.com/Europe/Italy/Inheritance

- Netherlands: The highest rate for spouses and children appears to be 20%. http://blog.clvn.nl/blog/2010/09/are-you-subject-to-dutch-inheritance-tax.html

- Switzerland: Highest rate in Canton of Geneva is 26%. Highest rates in many other canons are lower. http://www.globalpropertyguide.com/Europe/Switzerland/Inheritance

3. Non-tax problems that impact on U.S. estate tax planning.

   a. Who is the “Fiduciary” or Non-U.S. “Executor?” Many jurisdictions have very attenuated concept, if any, of “executor” to which U.S. assets can be transferred without U.S. probate.

      - Application of NY EPTL § 13-3.4 (“Payment or delivery of property to foreign fiduciaries”) is uncertain.

      - Transfer agents will often require U.S. federal “transfer certificate” and are generally unaware of the IRS “safe harbor” provisions under Treas. Reg. § 20.6325-1(b)(3).

   b. Problems in making foreign testamentary documents operate on U.S. Property.[3]

      - Lack of familiarity by U.S. courts with notarial and other forms of civil Wills

      - Difficulty in coordinating U.S. and non-U.S. property concepts:[4]

        ™ Universal heir vs. residuary estate

        ™ Usufruct vs. life estate

        ™ Lack of trust concept

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[3] See Galligan, “Buying USA: Ways of Minimizing U.S. Transfer Taxes on U.S. Property Interests of Non-U.S. Persons”, STEP USA (June 2007), http://www.phillipsnizer.com/pdf/Article-STEPJournalUSASupplementIssue3Galligan.pdf. (This article is also attached to this Outline as Exhibit B).

[4] See Galligan, “International Estate Planning for U.S. Citizens: An Integrated Approach,” 36 Estate Planning No. 10, 11 (October 2009), http://www.phillipsnizer.com/publications/articles/IntlEstatePlanIntegApproach_art.cfm.

™ Holographic wills vs. Witnessed Wills

™ Notarial Wills vs. Witnessed Wills

c. Possible Application of Non-U.S. Law

Subjecting assets to U.S. administration could subject intangible assets to forced heirship rules (because of U.S. choice of law rules), even though most U.S. jurisdictions do not themselves adopt compulsory inheritance rules.

4. U.S. Federal Taxes To Which Non-U.S. Persons can Be Subject

- Federal Estate Tax
- Federal Gift Tax
- Federal Generation-Skipping Transfer Taxes
- Federal Income and Gains Taxes

Be aware of matching or “tag along” state or municipal taxes in all these cases.

The Scope of the Federal Estate Tax

The estate tax under Subchapter A of Chapter 11 of Subtitle B only applies to the transfer of the estate of U.S. citizen decedents and U.S. “resident” decedents.

The estate tax on the transfer of estates of “nonresidents” who are not U.S. citizens is imposed by Subchapter B of Chapter 11 of Subtitle B and only applies to “that part of [their] gross estate (determined as provided in Section 2031) which at the time of their death is situated in the United States.”

The Scope of the Federal Gift Tax

The gift tax imposed by Chapter 12 of Subtitle B applies to the transfer of property by gift “by any individual resident or nonresident” with an exception for transfers of “intangible property by a nonresident not a citizen of the United States” (other than certain expatriates).

The Scope of the Generation-Skipping Transfer Tax

The GST Tax imposed by Chapter 13 of Chapter B applies to all “generation-skipping transfers,” including (i) direct transfers, (ii) certain trust distributions and (iii) certain trust terminations. However, by regulation § 26.2663-2(b), the GST Tax only applies to direct transfers or transfers in trust by a nonresident not a citizen of the United States that were subject in the first place to U.S. estate or gift tax.

The Scope of the Federal Income Tax

The income tax imposed by Subchapter A of Chapter 1 of Subtitle A is imposed on all married individuals, heads of household, surviving spouses, unmarried individuals, estates and trusts, and corporations.

“Nonresident Aliens”

Need to distinguish “non-resident aliens” for income tax purposes from “non-resident aliens” for transfer tax purposes:

Income Tax NRAs are generally individuals who are not lawfully admitted to the U.S. for permanent residency and do not meet the “substantial presence” test for U.S. income tax residence under IRC § 7701(b)(3).[5]

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[5] A foreign national is considered to be resident in the United States for U.S. federal income tax purposes (and thereby would be subject to U.S. income tax on his worldwide income) if he meets either of the “lawful permanent residence” test or the “substantial presence” test. [IRC § 7701(b)(1)(A)].

Under the lawful permanent residence test, the foreign national is considered resident in the U.S. from the day he enters the U.S. with a “green card” until the day that his “green card” status is revoked by the immigration authorities or that such status has been judicially determined to have lapsed. During the period that the foreign national maintains his “green card” status, he is considered to be resident in the U.S. for income tax purposes even if he is living at the time outside the U.S.

Under the “substantial presence” test, the foreign national is considered resident in the U.S. for U.S. income tax purposes if (1) he is present in the U.S. for at least 31 days during the current calendar year, and (2) he is present in the U.S. for a weighted average of at least 183 days over a three-year look-back period which includes the current calendar year and the two preceding calendar years (in determining the weighted average, all days present in the U.S. during the current calendar year are counted, but only one-third of the days present in the preceding year and one-sixth of the days present in the next preceding year are counted). Furthermore, in applying the “substantial presence” test, the foreign national must include any day on which he was present any time at all within the U.S.

Example One

Non-Resident

	2015	2016	2017	
Days	121	121	121	
Calculation	$20\,^{1}/_{16}$	$40\,^{1}/_{3}$	121 =	$181\,^{1}/_{2}$

Example Two

Resident

	2015	2016	2017	
Days	122	122	122	
Calculation	$20\,^{1}/_{3}$	$40\,^{2}/_{3}$	122 =	183

IRC § 872(a) limits the “gross income” of “nonresident alien individuals” (including estates and trusts pursuant to IRC § 641(b)) to only

- Gross income derived from sources within the United States that is not “ECI” income (IRC § 871(a)).[6] This is generally taxed at a flat 30% rate (or lower treaty rate) without the allowance of deductions. But note that certain categories of U.S. investment income such as interest on qualifying U.S. bank accounts and so-called “portfolio debt” as described in IRC § 871(h) is effectively exempt from tax under IRC § 871(a) provided that such interest does not constitute ECI.

- Gross income that is “ECI” – that is, “effectively connected with the conduct of a trade or business within the United States” (IRC § 871(b)). This is taxed at graduated rates on a net basis.

a. IRC § 882(b) applies the identical rules to “foreign corporations”

b. Generally, no capital gains tax on disposition of U.S. intangible property and tangible personal property not ECI, owned by persons who are not U.S. citizens or U.S. income tax residents. [But see IRC § 871(a)(2) where such capital gains are subject to U.S. income taxation in the case where the NRA is present in the U.S. for at least 183 days during the year (e.g., a foreign exchange student in the U.S. under an “F” or “M” visa).]

c. But capital gains tax is imposed on dispositions of U.S. real property interests (both direct interests in U.S. real property and U.S. corporations with substantial holdings of U.S. real property) owned by persons who are neither U.S. citizens nor U.S. income tax residents. See IRC § 897 (“FIRPTA”).

Note that there are several exceptions to the “substantial presence test” that allow certain categories of foreign nationals to avoid being treated as resident aliens even though their presence in the U.S. would satisfy the three-year look-back rule (for example, foreign government employees holding “A” visas, and, in certain instances, foreign exchange students holding “F” or “M” visas).

Further note that IRC § 7701(b)(3)(B) provides for an exception to the “substantial presence” test in the case of a foreign national who has 183 or more “deemed days” under the three-year look-back rule, but whose actual days present in the United States during the current calendar year is less than 183. The foreign national qualifies for this exception only if (1) he has a “tax home” in a foreign country for the current calendar year; (2) he has a “closer connection” with the same foreign country than he has with the U.S. for the current calendar year; (3) he does not have an application for “adjustment of status” pending at any time during the current calendar year, nor has he taken any actions to apply for a “green card”; and (4) he timely files with his U.S. income tax return, IRS Form 8840 or its equivalent disclosing to the IRS that that he qualifies for the IRC § 7701(b)(3)(B) exception.

[6] Two types of U.S.-source income are taxable under this category: 1) “fixed or determinable annual or periodical gains, profits, and income” (commonly referred to as “FDAP income”) taxed under IRC § 871(a)(1) and 2) U.S.-source capital gains, taxable under IRC § 871(a)(2), if the NRA was present in the U.S. for at least 183 days during the year of sale. (The HIRE Act of 2010 enacted the tax provisions of the so-called “Foreign Account Tax Compliance Act” (“FATCA”), which include provisions imposing U.S. withholding tax on certain “dividend equivalent” amounts paid or credited to non-U.S. persons on or after September 14, 2010.).

<u>Discussion</u>

Key Planning Issues:

I. What is the Citizenship of the Client?

To be treated as a non-U.S. person (and thus not subject to universal U.S. federal transfer taxes) a client cannot be a U.S. citizen.

Establishing U.S. Citizenship

A. Birth in the U.S. unless to non-U.S. diplomats.

B. Birth abroad to two U.S. citizen parents as long as one parent resided for a certain period in the U.S. or possession.

C. Birth abroad to a U.S. citizen and non-U.S. citizen depends on length of U.S. residence of U.S. citizen parent and age when such residence took place.

D. Birth of U.S. citizen to U.S. father out of wedlock requires some U.S. residence by father and legitimization or acknowledgement of paternity prior to age 18 of child.

E. Birth of U.S. citizen to mother out of wedlock requires mother to be physically present in U.S. or possession continuously 12 months before birth of child.

F. Naturalization.

G. Naturalization by parents if occurs before age 18.

H. Child Citizenship Act of 2000: at least one U.S. citizen parent and child admitted to U.S.A. as legal permanent resident if conditions are satisfied before age 18.

Helpful Reference:

<u>See</u> “Tables of Transmission Requirements Over Time for Citizenship for Certain Individuals Born Abroad,” Appendix B to Ira Kurzban, <u>Immigration Law Sourcebook</u> (Fifteenth Edition, 2016, AILA).

Note: Citizens Resident in U.S. Possessions

U.S. citizen who acquired U.S. citizenship solely by reason of

1. being a citizen of a U.S. possession by birth or

2. residence within a U.S. possession is considered a “non-resident not a citizen of the United States” for purposes of all taxes under Subtitle B (gift, estate, GST).

II. What is Domicile of the Client?

Note: To be treated as a non-U.S. person (and therefore subject to U.S. transfer taxes only on transfers of U.S. situs property), the client cannot be domiciled in the United States.

Meaning of “United States” To be a U.S. resident for U.S. transfer tax purposes, domicile must be established in one of the States of the United States or the District of Columbia.

A. Definition of Treas. Reg. § 20.0-1

“A person acquires a domicile in a place by living there, for even a brief period of time, with no definite present intention of later removing therefrom.”

1. Need intention to remain indefinitely

2. Intention to change not effective unless implemented

Thus, the definition of “domicile” clearly carries within it two necessary elements, those being (1) physical presence in a country and (2) intent to remain there indefinitely. Since physical presence is usually easy to determine, the essential element in determining domicile is whether taxpayer had intent to remain there indefinitely. The courts look to a variety of factors in gauging the intention of an individual to live in the U.S. with no definite present intention of relocating. It should be noted that while the case law provides helpful guidance, there is no bright line test in determining intent as every case has its own unique particulars and the issue of intent must be decided in the light of the facts peculiar to each case.

A typical list of factors that are considered in determining domicile include – but are not limited to – the duration of stay in the U.S. and in other countries, the relative nature, size, and cost of the individual’s residences, the location of the individual’s family, the location of the individual’s personal possessions, the location of the individual’s business interests, the place where the individual has stronger communal ties and maintains memberships in religious, professional, and social organizations, the location of bank accounts, declarations of residence or intent made in visa applications, wills, etc., and the individual’s motivations for being in the United States and being abroad

B. Notable Cases on Domicile

1. Estate of Nienhuys (47 T.C. 1149 (1952)) – Netherlands citizen declares to U.S. Immigration Authorities intent to reside permanently in U.S.A. and receives a “green card,” but is still found to be domiciled in The Netherlands (Tax Court found the particular facts convincing that the Netherlands citizen with a U.S. green card was not living in the U.S. by choice, but rather because Germany had invaded the Netherlands and that

he always hoped to return to The Netherlands if and when circumstances improved. He lived in a modest apartment in the U.S. though he could afford a higher-end residence which he continued to own in The Netherlands. His declaration on his visa applications were made while Germany was occupying the Netherlands).

2. Estate of Khan (T.C. Memo 1998-22 (1998)) – Pakistani citizen who lived his entire life in Pakistan (except for approximately seven years when he was residing in the U.S. and tending to his business and property interests which were more significant than the interests he held in Pakistan) and who died in Pakistan more than four years after he was last present in the U.S. is still found to be domiciled in the U.S. Tax Court found that, when decedent came to the U.S. on his last "tour of duty," he entered on a permanent resident visa, obtained a "green card" and social security number, and intended to stay to tend to his more significant business interests and that, when he left for Pakistan two years later (and never to return), he did so not to abandon his "U.S. domicile" but rather only to visit his family and to resolve some business matters. The court found that decedent's effort to obtain a U.S. re-entry permit at around the time of his departure to Pakistan was indicative that decedent did not intend to change his domicile from the U.S.

3. Estate of Jack (54 Fed. Cl. 590 (2002)) – Canadian citizen present in the U.S. and teaching at a California university on a temporary non-immigrant visa (in particular, a TN Temporary Professional visa) could be found to have established U.S. domicile for U.S. federal estate tax purposes despite the fact that an intent to remain permanently in the U.S. would violate the terms of his non-immigrant visa. Federal Claims Court ruled that the IRS should not be precluded from showing that decedent's domiciliary intent changed or was other than what he previously represented to immigration officials in his visa application. (But see, Carlson v. Reed, 249 F.3d 876 (9th Cir. 2001)).

An important "take away" from these cases and others[7] is that estate and tax planners must pay attention to practically every aspect of their clients' personal and professional lives in advising them as to how a U.S. court might rule on domicile.

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[7] Some other notable decisions include Estate of Paquette, T.C. Memo 1983-571 (1983); Estate of Fokker, 10 T.C. 1225 (1948); Elkins v. Moreno, 435 U.S. 647 (1978) (employees of international organization present in the U.S. on non-immigrant "G-4 visa" could still be found to be domiciled in the U.S. for U.S. federal estate tax purposes); Estate of Bloch-Sulzberger, 6 T.C.M. 1201 (1947).

C. Special Cases Where the Question of Domicile May Be Ambiguous

1. Persons who are considered domiciliaries of their country of nationality even after they have established domiciliary in different country (tax treaties).

   For example, under the U.S.-U.K. estate and gift tax treaty, a U.K. national (and domiciliary) who moves to the U.S. may still be deemed to maintain his domicile in the U.K. for a period of time after the move, at least if the U.K., under its own internal rules, considers the U.K. national to be a U.K. domiciliary for any period after his departure from the U.K. (See Article 4(2)(b) of such treaty, which provides that if such U.K. national had not been resident in the U.S. for Federal income tax purposes in 7 or more of the 10 taxable years ending with the year in which the death or transfer occurs, he may be deemed to be domiciled in the U.K. at that time).

2. Persons who have "green cards" but who do not have an intention to remain indefinitely in the U.S.

3. Persons who have conditional "green cards"

   a. Marriage to U.S. citizen

      A foreign national's permanent residence is conditional if it is based on a marriage that was less than 2-years old on the day such foreign national was given permanent residence. The foreign national could apply to remove the conditions on permanent residence if such foreign national is still married to the same U.S citizen (or permanent resident) after 2 years.

   b. Foreign National present in the U.S. under an EB-5 Visa.

      An EB-5 visa is a method of obtaining a green card for certain foreign nationals who invest money in the U.S. If the foreign national investor's visa application is approved, the investor and his dependents will be granted conditional permanent residence valid for two years Within 90 days before the conditional "green card" is set to expire, the investor must provide evidence showing that the full required investment has been made and that, as a result, a certain minimum number of jobs in the U.S. have been created or preserved or will be created within a reasonable time. If the investment fails, the foreign national must leave the U.S.

4. Former U.S. Citizens and Long-Term U.S. Residents who Expatriated Prior to June 17, 2008, the date that the new 2008 Expatriation Rules became effective under the HEART Act:

a) Persons who renounced U.S. citizenship or gave up “green card,” are deemed to have a tax-avoidance reason for doing so (10 year application)

b) Persons who spend substantial time in U.S. (10 year application)

Note: Do not confuse U.S. domicile with U.S. income tax residence:

1. A “green card” holder is subject to U.S. worldwide income tax regardless of plans to stay indefinitely or to leave after future occurrence

2. Application of “days test” is mechanical except for narrow exception under IRC § 7701(b)(3)(B)

III. What Property Does A Client Own And What Is Its Nature?

A. What Are The Forms Of Ownership That Count?

1. Distinction Between Legal Title and Beneficial Ownership

Title: Trust, Stiftung, Corporate Nominee…

Beneficial: Trust Beneficiary, Foundation Distributee, Beneficial Owner of Assets Held in Corporate Name …

Treas. Reg. § 20.2013-5(a)

> “. . . the term “property” means any beneficial interest in property, including a general power of appointment . . . over property. Thus, the term does not include an interest in property consisting merely of a bare legal title . . .”

Special Cases:

- Application of IRC § 2104(a): Stock “owned and held” by a nonresident noncitizen of the U.S. (“NRNC”) subject to U.S. estate tax only if issued by U.S. corporation. However, stock of a foreign corporation is not includible in the U.S. estate of a NRNC, regardless of whether the stock certificates are actually located within the U.S. [See Treas. Reg. § 20.2105-1(f)].

  See Estate of Charania v. Shulman, 608 F.3d 67 (1st Cir. 2010), aff’g in part, 133 T.C. 122 (2009) (stock of Citigroup held subject to U.S. estate tax, undiminished by alleged community property share of surviving spouse).

  American Depositary Receipts (“ADRs”), although normally issued and sold by U.S. banks are considered to have situs outside the U.S. because they substantively are treated as shares in foreign corporations. [See PLR 200243031].

Investments in U.S. real property owned by Canadian mutual funds that were a part of NRNC decedent's RRSP held not includible in NRNC decedent's U.S. estate because the Canadian mutual funds were determined to have foreign situs as they were properly classified as corporations incorporated outside the United States. [See CCA 201003013].

* Risk of non-U.S. corporations holding U.S. assets being considered nominees for their shareholders: See Fillman v. U.S., 355 F.2d 632 (Ct. Cl. 1966)

  The situs rule for stock of foreign corporations has resulted in the use of foreign holding corporations as a major estate planning tool to prevent assets of a NRNC, which would otherwise have U.S. situs if held directly, from being subject to U.S. federal estate tax. The Fillman case strongly cautions planners that more is required than simply placing U.S. situs assets in a foreign corporation. At a minimum, the corporation should be in good standing under local law and corporate formalities should be followed.

* Risk that, in certain circumstances, a transfer of U.S. stock to a foreign holding company may cause the foreign holding company (“inverted” or “surrogate foreign corporation”) to be treated under, IRC § 7874(b), as a U.S. corporation for all tax purposes under the Internal Revenue Code, notwithstanding IRC § 7701(a)(4).

- Application of IRC § 2104(b): Trusts funded with U.S. property or holding U.S. property upon death of NRNC settlor in which NRNC settlor has retained right of enjoyment or incidents of control treated as de facto nominee for U.S. assets held by trust or attributable to U.S. property with which trust was funded upon death of NRNC settlor. [See TAM 9507044 (February 17, 1995) (trust funded with U.S. property).].

* Risk that non-U.S. partnerships and non-U.S. LLCs holding U.S. assets, if otherwise qualifying as non-U.S. assets, may be considered nominees for their partners holding U.S. assets See Matter of Strangi, TC Memo 2003-145 (2003), aff'd 417 F.3d 468 (5th Cir. 2005)

B. What Property Does the Client Share with Others?

1. Matrimonial Property Regimes

a. Separate Property

b. Community Property as to Marital Property

c. Community Property as to All Property of the Spouses

Special Cases:

1. Germany: Separate Property with "Community of Surplus."[8]

2. New Zealand Matrimonial Property Law.

3. United States: Spousal Right of Election.

Note: New York has adopted the New York Uniform Disposition of Community Property Rights at Death Act. N.Y. EPTL §§ 6-6.1 through 6-6.7.

2. Forms of Common Law Joint Ownership (Tenants by Entirety, Joint Tenants with Survivorship) as distinguished from Tenants in Common.

U.S. Citizen Spouses: Property assumed owned 50/50 for Federal Estate tax purposes.

Non-U.S. Citizen Spouses

One or Two Non-citizen Spouses:	Property subject to estate tax based on contribution.
Gifts of real property:	Contribution rule for gift tax purposes is applied on distribution of proceeds of sale.
Gifts of intangible property:	Contribution rule for gift tax purposes is applied when joint interest is established.[9]

See Estate of Charania v. Shulman, 608 F.3d 67, 73 (1st Cir. 2010), aff'g in part, 133 T.C. 122 (2009) – The estate of the deceased U.K. NRNC

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[8] "Zugewinngemeinschaft."

[9] See Dina Kapur Sanna, "Unexpected Gift Tax From Joint Accounts With Foreign Spouse," Estate Planning Journal (December 2011).

who owned stock of Citigroup directly, argued that one-half of the stock was owned by surviving spouse as community property; couple did not take steps under Belgian law to declare a community property regime and U.K. precedent applicable to NRNC did not consider change of matrimonial domicile from separate property jurisdiction (Uganda) to Belgium sufficient to effect change from separate property to community property.

Note: Non-Citizen Spouses

- Enlarged annual exclusion for gifts of "present interests" to non-U.S.-citizen spouse: The exclusion is indexed for inflation and is currently at $139,000 for 2012.
- No QDOT Trust is available for lifetime gifts to non-U.S. citizen spouse.
- If either or both spouses are NRNCs, no "gift-splitting" (attributing the gift of one spouse to both spouses to maximize utilization of gift tax exclusions and exemptions) not permitted. IRC § 2513(a)(1).

C. What Property Owned by Client Might be Subject to Claims of Others?

1. "Clawback Provisions" under Forced Heirship Statutes

<u>Spain</u>:	No statutory limit on look-back to transfers made during lifetime (but limitations may be supplied by courts)
<u>Switzerland</u>:	Look-back for most part, limited to five years
<u>France</u>:	Surviving spouse may withdraw gifts made to predeceased spouse

2. Testamentary Substitutes Under Spousal Right of Election

a. Unlimited look-back (subject to enactment dates) for transfers into trust with retained interest. NY EPTL § 5-1.1-A(b)(1)(F)

b. One year look-back for all direct gift transfers. NY EPTL § 5-1.1-A(b)(1)(B)

Note: Spousal right of election in New York is not available to spouse of non-New York domiciliary decedent unless decedent made an election to have disposition of New York property governed by New York law under EPTL § 3-5.1(h).

D. What Property of Client Is Subject to Creditors' Claims?

1. In many civil law jurisdictions, heirs (absent express election to contrary) take decedent's property, subject to unlimited liability for decedent's debts.

2. In New York, generally, claims of creditors of decedent limited to estate assets but an heir can also be liable for debts to the extent of property received from estate for debts not satisfied from assets subject to administration (NY EPTL § 12-1.1).

IV. Where Is Client's Property Located?

A. For Purposes of Determining Applicable Inheritance Law

1. Civil Law Tradition Generally:

a. No Distinction Between Real and Intangible Property (No "Scission")

b. Applicable Law is Based on Citizenship

c. Is the applicable law the "Whole Law" (or "Substantive Law" only)?

Germany (yes)

Italy (probably yes)

Spain (no – but there may be different views)

d. "Renvoi" from the Country of Citizenship increasingly applied

2. Common Law:

a. Distinction between real property and intangible property ("scission")

b. Real property governed by law where property is located

c. Intangible Property governed by law of domicile or owner (individual or trustee); "mobilia sequuntur personam" ("moveable assets follow the person").

Mixed Situations

- France

    - Recognizes Scission.
    - Immoveable property follows law of situs.
    - Moveable property follows law of domicile.
- Switzerland
    - Generally, does not recognize scission
    - Habitual residence rather citizenship is key factor

B. For Purposes of New York EPTL § 3-5.1(h) and EPTL § 7-1.10

- Real property and tangible property located in New York

Bank and Brokerage Accounts with New York branches of banks and brokerage houses. See Hutchinson v. Ross, 262 N.Y. 381 (1933) (Quebec domiciliaries) ("Tangible chattels and securities") – not following rule of "mobilia sequuntur personam;" Wyatt v. Fulrath, 38 Misc. 2d 1012 (1963) (Spanish domiciliaries) (joint bank accounts).

- Entities organized by New York and physical documents maintained here

C. For purposes of N.Y. EPTL § 7-1.10

"Whenever a person, not domiciled in this state, creates a trust which provides that it shall be governed by the laws of this state, such provision shall be given effect in determining the validity, effect and interpretation of the disposition in such trust of:

1) Any trust property situated in this state at the time the trust is created

2) Personal property, wherever situated, if the trustee of the trust is a person residing, incorporated or authorized to do business in this State or a national bank having an office in this State."

In re Tabbaghi's Estate, 167 Misc. 156 (1938) (France) (validity of trust)

D. For purposes of N.Y. EPTL § 3-5.1(h)

"Whenever a testator, not domiciled in this state at the time of death, provides in his will that he elects to have the disposition of his property situated in this state governed by the laws of this state, the intrinsic validity, including the testator's general capacity, effect, interpretation, revocation or alteration of any such disposition is determined by the local law of this state."

See Estate of Renard, 56 N.Y.2d 973 (1982) (bank and brokerage accounts)

E. For Purposes of U.S. Federal Gift Tax and Gift-Related GST Tax

1. Real Property Located in U.S. treated as U.S. situs. [See Treas. Reg. § 25.2511-3(b)].

   * Possibility of gifts of non-U.S. cash by NRNC intended to facilitate purchase of U.S. real property could be characterized as real property itself, under IRS "step transaction" theory. [See Goldschmidt-Rothschild v. Commissioner, 168 F.2d 975 (2d Cir. 1948); Davies v. Commissioner, 40 T.C. 525 (1963).].

2. Tangible Personal Property located in U.S. treated as U.S. situs. [See Treas. Reg. § 25.2511-3(b)].

   * Vexed issue about funds in U.S. bank deposit accounts for U.S. gift tax purposes

   A gift by an NRA by means of a check drawn against his U.S. bank account or a wire transfer to a donee's U.S. account may be treated as a gift of currency, in which case, it would likely be treated by the IRS as a gift of tangible personal property located in the U.S. [See Treas. Reg. § 25.2511-3(b)(4)(iv); PLR 7737063; GCM 36860 (Sept. 24, 1976); Rev. Rul. 55-143].

   An NRA who desires to make a cash gift and avoid IRS potentially characterizing it as a taxable gift should not issue a check on a U.S. bank account or wire funds from a U.S. bank account, but rather should wire funds from his offshore account to offshore accounts held by the U.S. donees or should withdraw cash from a U.S. account and give out the cash to the U.S. donees outside the U.S.

3. Intangible Personal Property with U.S. connections treated as foreign situs. For example, a gift of U.S. corporate stock by a non-resident alien is exempt from gift tax even if the stock certificate is physically located in the U.S. [See IRC § 2501(a)(2)].

F. For Purposes of U.S. Federal Estate Tax and Estate-Related GST Tax

1. Real Property Located in the United States has U.S. situs. [See Treas. Reg. § 20.2104-1(a)(1)].

   Note: Remember that "real property" under common law has a narrower definition than "immovable property" under civil law

2. Tangible Personal Property

Tangible Personal Property that is not being used or loaned for exhibition or related purposes and that is located in the United States has U.S. situs. [See Treas. Reg. § 20.2104-1(a)(2)].

Note: Currency is treated as tangible personal property for estate tax purposes. [See Rev. Rul. 55-143].

3. Shares of Stock of U.S. Corporations

Shares of stock issued by a U.S. "domestic" corporation (regardless of location of certificates) have U.S. situs. [See IRC § 2104(a); Treas. Reg § 20.2104-1(a)(5)].

a. IRC § 2104(a) refers to shares "owned and held" by an NRA.

b. Treas. Reg. § 20.2104-1(a)(5) omits the reference to "owned and held."

c. Note: A transfer tax treaty may override the Code's inclusionary rule as to stock of U.S. corporations. For example, generally, under the "modern" U.S. estate tax treaties (for example, treaties with the United Kingdom, France, Germany, and The Netherlands), the U.S.'s treaty partner has the exclusive right to tax stock in U.S. corporations where the decedent is determined to be a domiciliary of such treaty partner.[10]

d. For an estate of a NRNC decedent who died after 2004 and before 2012, if such NRNC decedent had owned stock of a U.S. mutual fund or "regulated investment company" (i.e., "RIC"), only the proportion of the fund invested in U.S. situs assets are subject to U.S. estate tax. IRC § 2105(d). The purpose of this rule was to provide an exemption to the estates of foreign persons who invest in certain assets through a RIC to the same extent that those assets would not be subject to the estate tax if held directly. However, for NRNC decedents dying in 2012 and thereafter, the exception of IRC § 2105(d) is no longer applicable and shares in RICs (i.e., domestic mutual funds) are fully includible in the U.S. estate of a NRNC by virtue of IRC § 2104(a)

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[10] See Galligan, "Making Sense of Four US Estate Tax Treaties: US-Netherlands, US-Germany, US-France, US-UK," NYSBA International Law Practicum (Spring, 2004), http://phillipsnizer.com/pdf/Article-MG-4TransAtlanticTaxTreaties-Spring04.pdf. See also Glenn G. Fox, "U.S. Estate Planning for Nonresident Aliens from Treaty Countries: A Comparison of Germany, Austria, France and the United Kingdom," http://www.alston.com/files/Publication/8e33adc5-35ec-44c6-b393-15a5eb07710e/Presentation/PublicationAttachment/f41b0875-0670-48ce-9790-9ca67f1ae75d/FoxBNA%20Article%20on%20Estate%20and%20Treaty%20Planning%20for%20NRAs.DOC

4. Debt Obligations of U.S. Persons

Debt obligations of a U.S. person, the U.S. or a political subdivision if not treated as "outside the U.S." by IRC § 2105 have U.S. situs.

a. In the case of NRNCs who <u>are not</u> U.S. income tax residents, debt obligations that have U.S. situs include:

   (i) Portfolio debt issued on or prior to July 18, 1984

   (ii) Debt issued by companies in which the NRC held 10% or more of the voting power (corporation) or capital or profits interest (partnership) [IRC § 871(h)(3)(B)].

   (iii) Obligations issued by state and local municipalities[11]

   (iv) Obligations subject to profitability or similar contingencies [IRC § 871(h)(4)(A)].

   (v) Bearer bonds described in IRC § 163(f)(2)(B) and are issued on or after March 19, 2012.

b. In the case of NRNCs who <u>are not</u> U.S. income tax residents, the following debt obligations have foreign situs:

   Debt obligations that are portfolio debt obligations (except for those enumerated in (i) through (v) above) are generally foreign situs, even if issued by a U.S. person, if issued after July 18, 1984. [IRC § 2105(b)(3)]. This generally applies to debt obligations if any interest thereon would be eligible for the exemption from U.S. income tax under IRC § 871(h)(1) were such interest received by the NRA decedent at the time of his death, without regard to whether the U.S. issuer has received a statement (that satisfies the requirements of IRC § 871(h)(5)) that the beneficial owner of the obligation is not a U.S. person. The term "portfolio interest" also includes interest that is paid on a non-registered obligation (like a bearer bond) that was issued before March 19, 2012 and that is described in IRC § 163(f)(2)(B). Debt obligations considered as having foreign situs, for decedents dying after August 5, 1997, also include short-term obligations (OID) with maturity dates of 183 days or less as long as any interest thereon is not effectively connected with a U.S. trade or business. [IRC § 2105(b)(4)].

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[11] Due to the technicality that the IRS § 871(h) income tax exemption only applies if interest is exempt only by virtue of IRC § 871 (but "query" whether such income is exempt under general principles of U.S. tax law).

c. In the case of NRNCs who are U.S. income tax residents, all U.S. debt obligations have U.S. situs – because U.S. income tax residents are not eligible for the exemptions described in IRC § 871(h).[12]

5. Certain Deposits

a. A NRNC's deposit with a domestic bank is not considered to have a U.S. situs as long as the deposit is not effectively connected with a trade or business conducted by the NRNC within the U.S. [IRC § 2105(b)(1)]. Additionally, a deposit in an offshore branch of a U.S. domestic bank is also deemed to have a foreign situs. [IRC § 2105(b)(2)].

Any conventional bank deposit (for example, funds in checking and savings accounts and in certificate of deposits) are considered under the above rule of IRC § 2105(b) to have foreign situs.

In PLR 200842013, the IRS ruled that annuity proceeds due a NRNC decedent, but still held by the insurance companies as of the decedent's death, were not deemed to have U.S. situs pursuant to IRC § 2105(b)(1) and therefore were excluded from NRNC's gross estate under IRC § 2103.

b. The following deposits have U.S. situs:

Special deposits held by U.S. banks in a custodial capacity that are not commingled with other assets of the bank. [See Rev. Rul. 69-596].

Deposits with brokerage houses

Deposits with U.S. branches of foreign corporations that are engaged in the commercial banking business (and do not fit within the portfolio interest exclusion)

6. Other Intangible Property

"Intangible Personal Property, the written evidence of which is not treated as being the property itself, if it is issued by or enforceable against a U.S. resident or a domestic corporation or governmental entity." Treas. Reg. § 20.2104-1(a)(4)

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[12] Further details on inclusion and exclusion of debt instruments as well as on many other topics related to U.S. estate tax planning for NRNCs may be found in Michael A. Heimos, 837-3rd Tax Management Inc., Non-Citizens – Estate, Gift and Generation-Skipping Taxation.

a. “Property the written evidence of which is treated as being the property itself” was thought to include bonds for the payment of money (see Treas. Reg. § 20.2104-1(a)(3))

b. “U.S. resident” is presumably defined as U.S. domiciliary.[13]

c. Possible Application:

  (i) Partnerships

  (ii) Limited Liability Companies

  (iii) Intellectual Property Rights

  (iv) License rights

Special Note on Partnerships

(a) Often thought of as intangible personal property

(b) General partners generally have rights to terminate partnership and therefore may be seen as owning shares of the underlying partnership property

See Sanchez v. Bowers, 70 F.2d 715 (2nd Cir. 1934)

(c) Rev. Rul. 55-701 (situs is where partnership does business) should not be applicable

  a. Decided under superseded U.S.-U.K. Estate Tax Convention

  b. Treas. Reg. § 20.2104-1 was amended in 1973 and 1974 and did not adopt this rule

(d) “Look-through” rule of Sanchez v. Bowers, 70 F.2d 715 (2d Cir. 1934) generally applied only to general partnerships or perhaps interests of general partners in limited partnerships.

(e) Case for applying the rule of Blodgett v. Silberman, 277 U.S. 1 (1928) uses the common law ‘domicile of decedent rule’ for situs of intangible property. How strong is this position?

  (i) Depends on contention that Treas. Reg. § 20.2104-1(a)(4) was not intended to apply due to the language therein suggesting that it has limited applicability

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[13] Treas. Reg. § 20.2104-1(a)(7) refers by contrast, to U.S. person as defined in IRC § 7701(a)(30) for U.S. income tax purposes

or

(ii) Depends on contention that Treas. Reg. § 20.2104-1(a)(4) is "ultra vires" because it addresses issues not explicitly addressed by IRC § 2104.

Important Principle:

"State law creates legal interests and rights. The federal revenue acts designate what interests and rights, so created, shall be taxed."

Morgan v. Commissioner, 309 U.S. 78, 80 (1940)

Therefore, only express departures from state law concepts by Federal tax law regarding situs of property should be valid.

Special Note on Limited Liability Companies

(a) In the absence of an election to the contrary, a U.S. LLC is treated for all U.S. tax purposes as a partnership if it has two or more members. Treas. Reg. § 301.7701-3(b).

(b) In the absence of an election to the contrary, a single-member LLC is disregarded.

(c) In the absence of an election to the contrary, a non-U.S. LLC is treated for U.S. tax purposes as a partnership if it has two or more members and one member does not have limited liability.

(d) LLCs generally did not exist under U.S. law in 1955 – therefore even better argument that Rev. Rul. 55-701 does not apply.

(e) Sanchez v. Bowers should not apply when there are no "general partners."

(f) LLCs were still rare in early 1970's when Treas. Reg. § 2104-1(a)(4) was last amended.

(g) Argument in favor of applying the Blodgett rule attributing situs to domicile of owner of LLC interest may be stronger than with a partnership interest.

7. Trusts

"Look-through" Rules for Trusts

(i) U.S. property transferred "in trust or otherwise" in which decedent retained an interest (under IRC §§ 2035 through 2038) at the time of death (IRC § 2104(b)).

(ii) Property (even non-U.S. property) held "in trust or otherwise" that originated from U.S. property transferred to the trust by the decedent (IRC § 2104(b)).

(iii) Non-U.S. situs share of property held by a U.S. regulated investment company ("RIC") (2005-2011) is eligible for exclusion.

Cases and Rulings

<u>Swann v. Commissioner</u>, 247 F.2d 144 (2d Cir. 1957): Stiftung treated as a U.S. trust with retained interest despite provisions of U.S.-Switzerland income tax treaty treating Stiftung as corporation.

TAM 9507044 – Trust created in 1923 with U.S. assets subject to U.S. estate tax even though assets in trust when grantor died in 1991 had non-U.S. situs.

But see CCA 201020009 (payment of gift tax within 3 years of NRNC decedent's death considered made under IRC § 2035(b) is not a transfer within the meaning of IRC §§ 2035 to 2038; thus such gift tax paid is not property deemed situated in the U.S. under IRC § 2104(b))

V. What Planning Entities Work Best for Client?[14]

A. Corporations

1. Consider Treas. Reg. § 20.2105-1(f)

> "Shares of stock issued by a corporation which is not a domestic corporation, regardless of the location of the certificates" are treated as outside the U.S.

2. Consider whether the stock of foreign corporation must be "owned and held" by non-U.S. shareholder.

3. Avoid having the corporation be treated as a nominee for foreign shareholder. See <u>Fillman v. U.S.</u>, 355 F.2d 632 (Ct. Cl. 1966).

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[14] For an overview, see the discussions in Robert F. Hudson, Jr., "The U.S. Tax Effects of Choice of Entities for Foreign Investment in U.S. Real Estate and Businesses and the Taxation of Dispositions of U.S. Partnership Interests," http://www.iirusa.com/upload/wysiwyg/U1986/IIR_U1986_Hudson.pdf; Richard Lehmann, "United States Taxation of Foreign Investors," http://www.lehmantaxlaw.com/unitedstatestaxation.html; Cassell, Karlin, McCaffrey & Streng, "U.S. Estate Tax Planning for Nonresident Aliens Who Own Partnership Interests," http://www.bryancave.com/files/News/051c9ea8-18a6-4d16-84d2-8aee4410f817/Presentation/NewsAttachment/051ab378f-4ab5-8540-8c6edfe6e2c5/RCassell%20article.pdf

4. Consider U.S. income tax consequences if foreign corporation holds U.S. assets directly

   a. Corporate capital gains tax rates on sale of U.S. real property (FIRPTA)

   b. Possible branch profits tax on U.S. business activities, not applicable at least in cases where sole asset of foreign corporation is U.S. real estate that does not generate income, or where income is reinvested in the real estate, as long as corporation is liquidated soon after sale of real estate.

      If foreign corporation is in a treaty jurisdiction, treaty may provide branch profits tax relief.

   c. Possible loss of tax treaty benefits if foreign corporation is in a tax haven jurisdiction.

5. Consider U.S. income tax consequences if direct owner of U.S. assets is U.S. corporation owned by foreign corporation.

   a. Corporate capital gains tax rates on sale of all U.S. assets

   b. No branch profits tax

   c. U.S. withholding tax on payment of dividends to foreign corporate parent, subject to reduced treaty rates depending on residence of foreign corporation; no such withholding tax if earnings are reinvested and paid out to foreign corporate parent upon liquidation of U.S. corporation after payment of U.S. capital gains tax on sale of assets it holds.

6. Consider non-U.S. income tax consequences, especially if corporation is not organized in client’s primary tax jurisdiction.

7. Consider U.S. tax consequences if corporate stock is later owned by U.S. persons:

   (a) Loss of step-up in basis for assets held by corporation

   (b) Treatment of foreign corporation if treated as CFC or PFIC

B. Partnerships and LLCs Qualifying as Partnerships[15]

1. U.S. Partnership still may be vulnerable to U.S. estate tax inclusion (Risk)

2. Foreign Partnerships may be vulnerable to U.S. estate tax inclusion if engaged in U.S. business activities (Risk)

3. Share of U.S. Capital Gains taxed at Individual Rates (Advantage)

4. Availability of IRC § 754 election to "step-up" internal basis of partner's share of underlying assets to match the post-death external basis. (Advantage)

5. No U.S. NRA withholding tax; tax treaty benefits may be more accessible; and no branch profits tax (Advantage).

6. If primary taxing jurisdiction accepts partnership treatment, may be more acceptable to that jurisdiction (Advantage).

7. Would not be treated as CFC or PFIC if passes to U.S. owners (Advantage).

C. Consider Combination of U.S. LLC and Foreign Corporation

a. LLC organized in U.S. jurisdiction could establish U.S. situs for non-tax purposes but be disregarded for U.S. tax purposes if owned by sole foreign person.

b. Corporation not owned abroad but owned by LLC would still be treated as owner of assets for U.S. tax proposes.

c. Possible approach to combining benefits of U.S. tax planning for non-U.S. person, with protection from foreign property law issues under EPTL § 3-5.1(h) and/or EPTL § 7-1.10. (See Exhibit A).[16]

U.S. assets owned by non-U.S. corporation

Non-U.S. corporation owned by single-member N.Y. LLC

Single member of LLC is either:

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[15] Note that, under Rev. Proc. 2012-7, the IRS will not issue rulings as to whether a partnership interest is intangible property for purposes of gifts by NRNCs and therefore will not be subject to U.S. gift tax, pursuant to IRC § 2501(a)(2).

[16] For further discussion of these provisions of New York law, see Galligan, "Forced Heirship in the United States of America," in these materials for the Eighth Annual NYSBA-STEP International Estate Planning Institute.

… Non-U.S. individual with Will directing application of N.Y. law to N.Y. property

or

N.Y. trust directing that N.Y. law govern the trust.

D. Insurance

Wrapping U.S. property in insurance vehicles that qualify as insurance for U.S. tax purposes and where the insurance is on the life of the owner of the policy.

Life insurance on the owner of the policy as source of funding for assets that have to be owned directly by non-U.S. person (no U.S. estate planning need for irrevocable life insurance trust because of life insurance exclusion under IRC § 2105(a)).

VI. What To Do When The Client Has Already Acquired U.S. Property In Client's Own Name?

A. Gifts

Lifetime gifts of intangible U.S. property, including stock of U.S. corporations, U.S. partnership interests, notes, intellectual property rights, claims are all exempt from U.S. gift tax.

Lifetime gifts of real and tangible property located in the United States do not provide very much relief since there is no lifetime gift tax exemption for NRNCs. [IRC § 2505(a).] Annual exclusion is available (currently $13,000 per donee) but this is not likely to be of much avail. Gift tax exclusion of educational and medical expenses may be helpful when cash gifts are made from U.S. accounts, granted some uncertainties about the characterization of funds from such accounts as tangible or intangible property, but hardly help with problems involving U.S. real estate or U.S. tangible property that a NRNC may own directly. [IRC §§ 2503(b) & (e)].

B. Exchanges of U.S. assets for stock or membership interest in a non-U.S. entity (Generally, no U.S. capital gains tax on sale or exchange of U.S. intangible property and tangible property by person who is neither U.S. citizen nor U.S. income tax resident; see also IRC § 351(a) and IRC § 721(a) non-recognition rules).

<u>Caution</u>: Plan to avoid potential application of IRC § 7874(b) to cause the foreign corporation to be treated as a domestic corporation for U.S. tax purposes.

IRC § 7874(b) applies where stock in a U.S. corporation (or the U.S. assets of a U.S. corporation) are transferred to a foreign holding company whereby (1) the

U.S. corporation becomes a subsidiary of such foreign holding company (or substantially all of the U.S. assets of the U.S. corporation are now held by the foreign holding company); (2) the former shareholders of the U.S. corporation hold at least 80% of the foreign holding company's stock by vote or value after the transfer; and (3) the foreign holding company and its "expanded affiliated group" do not have substantial business activities in the foreign country where the foreign holding company is organized.

C. U.S. Real Property Interests ("USRPI")

Capital Contribution of USRPI to foreign corporation subject to tax. IRC § 897(j)

Exchange of direct interest in real property for stock of foreign corporation will trigger tax. IRC § 897(e)(1) and Temp. Reg. § 1.897-6T(b)(3).

Possibility under certain circumstances of deferral of tax on exchange of interest in U.S. Real Property Holding Corporation ("USRPHC") for stock of a foreign corporation. Temp Reg. § 1.897-6T(b)(1).

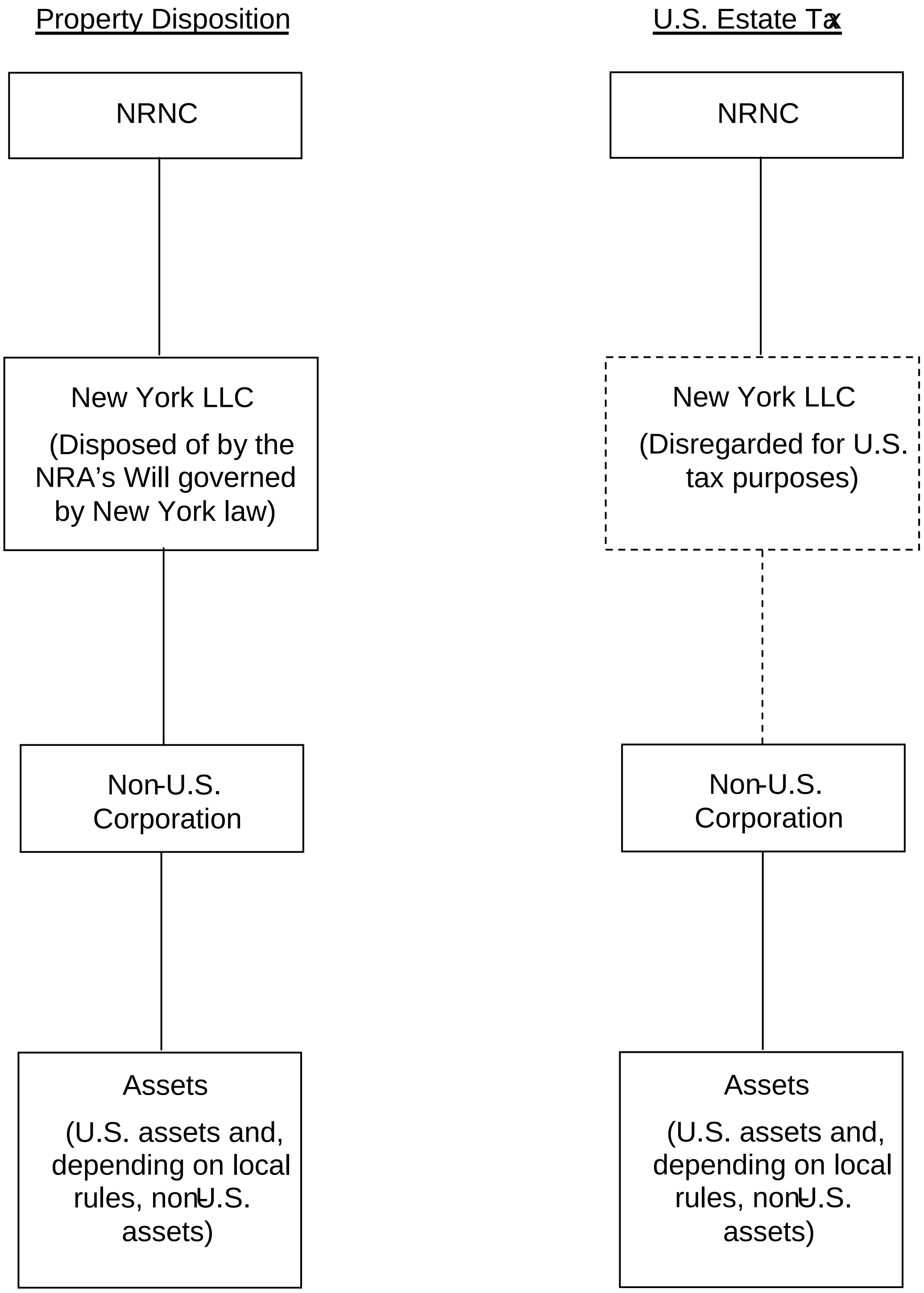
Exchange of direct interest in U.S. real property or an interest in a USRPHC eligible for nonrecognition under IRC § 721 subject to potential recognition under IRC § 897(e) but Temp. Reg. § 1.897-6T(a)(3) provides:

> "For example, the exchange of a U.S. real property interest for an interest in a partnership will receive non-recognition treatment . . . only to the extent that a disposition of the partnership interest will be subject to U.S. taxation by reason of the operation of Section 897(g)."

Another approach to Real Property: encumber real property with non-recourse debt.

Exhibit A

U.S. NRNC Estate Planning
Under New York EPTL Section 3-5.1(h)



MAJOR U.S. TAX TYPES OF DISCLOSURE FOR U.S. INDIVIDUAL TAXPAYERS WITH NON-U.S. SOURCE INCOME AND INVESTMENTS: FORMS AND POTENTIAL TAX REGIMES

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A. Interests in non-U.S. financial accounts where the aggregate maximum value of such accounts exceeds $10,000 at any time during the calendar year – FINCEN Form 114 – commonly referred to as the "FBAR" form[1]

1. Direct ownership of interests in non-U.S. financial accounts (broadly defined – not limited to "bank accounts")

2. Indirect ownership – some examples where U.S. owner/beneficiary must also include accounts owned by an entity

   Corporation in which U.S. Person owns directly or indirectly more than 50% of voting power or share value

   Grantor trusts

   Trust in which U.S. person has a greater than 50% present beneficial interest in the assets or income of the trust

3. Signature authority over non-U.S. financial accounts

   "Signature authority" is the authority of an individual (alone or in conjunction with another individual) to control the disposition of assets held in a foreign financial account by direct communication (whether in writing or otherwise) to the bank or other financial institution that maintains the financial account.

B. Interests in specified foreign financial assets (e.g., non-U.S. financial accounts, securities and entities) – IRS form 8938

1. <u>Unmarried taxpayers</u> total value of such assets is more than $50,000 at end of tax year or more than $75,000 on any day during tax year

2. <u>Married filing jointly</u>: total value of such assets is more than $100,000 at end of tax year or more than $150,000 on any day during tax year

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[1] The information in this presentation is provided for educational purposes only and does not constitute the rendering of tax, legal, or other advice from Phillips Nizer LLP or any of its members. The information in this presentation should not be used as a substitute for obtaining competent tax or legal advice from an experienced licensed attorney with whom you have entered into an attorney-client relationship.

3. Married filing separately: same as unmarried taxpayers

4. Note that thresholds are higher for U.S. taxpayers residing outside the USA

    Filing other than a joint return: total value of such assets is more than $200,000 at end of tax year or more than $300,000 on any day during tax year

    Married filing jointly: total value of such assets is more than $400,000 at end of tax year or more than $600,000 on any day during tax year

IRS form 8938 pertains to

    Any financial account held at a foreign financial institution (but not if held at U.S. branch of such institution)

    Stock or securities issued by non-U.S. persons

    Interest in a foreign entity

    Cash value life insurance or annuity contracts issued by non-U.S. persons

    Financial instrument with issuer or counterparty who is not a U.S. person[2]

C. Interests in non-U.S. mutual funds and other forms of so-called “passive foreign investment companies” (“PFICS”) — IRS form 8621

A foreign corporation is a “PFIC” if it satisfies either of the following two tests:

1. Asset test: 50% or more of the average value of the foreign corporation’s gross assets consist of assets that would produce passive income; or

2. Income test: 75% or more of the foreign corporation’s gross income is passive as generally defined in accordance with the foreign personal holding company income rules

D. Interests in “controlled foreign corporations” (“CFCs”) — IRS form 5471 (Category 5 filer) (Subpart F income and earnings invested in U.S. property)

1. A foreign corporation is a “CFC” where more than 50% of value or voting power of such corporation is owned collectively by “United States Shareholders”

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[2] The IRS recently revised the reporting requirements for Form 8938 to provide that a U.S. income tax resident who, on the last day of the taxable year, is considered a non-U.S. resident because he or she has claimed, based on the provisions of a U.S. income tax treaty, to be a resident of the Treaty partner, is not required to file a Form 8938 with respect to the portion of the tax year he or she is treated, for U.S. income tax purposes, as a resident of the other country, as long as he or she has filed a U.S. Non-Resident Return (Form 1040NR or Form 1040NR-EZ) for such period.

2. “United States Shareholder” is a U.S. person who directly, indirectly, or constructively owns 10% or more of the voting power of the foreign corporation.

E. Interests in certain other foreign corporations – IRS form 5471

1. A U.S. person who is an officer or director of a foreign corporation in a year in which any U.S. Person (a) acquired stock causing such person to own 10% or more of the value or voting power of such corporation or (b) acquired an additional 10% or more of the value or voting power of such corporation - (Category 2 filer)

2. A U.S. Person who during the year being reported (a) acquired stock causing such person to own 10% or more of the value or voting power of a foreign corporation or (b) acquired an additional 10% or more of the value or voting power of a foreign corporation - (Category 3 filer)

3. A non-U.S. Person who during the year being reported became a U.S. person while meeting the 10% foreign corporation stock ownership requirement – (Category 3 filer)

4. A U.S. Person who during the year being reported disposed of stock of a foreign corporation causing such person’s stock ownership in such corporation to fall below 10% - (Category 3 filer)

5. A U.S. Person who had “control” of a foreign corporation for an uninterrupted period of at least 30 days during such corporation’s annual accounting year ending within such U.S. person’s taxable year. (“Control” means ownership of more than 50% of the value or voting power of foreign corporation) – (Category 4 filer.)

6. A U.S. Person who qualifies as a U.S. Shareholder of a CFC (see D (1)&(2) above for definitions -(Category 5 filer).

F. Interests in certain foreign partnerships – IRS Form 8865

1. “Control” of a foreign partnership by U.S. person (“control” means ownership of more than 50% interest) – (Category 1 filer)

2. Ownership by U.S. person of 10% or greater interest in foreign partnership when such partnership is collectively “controlled” (as defined above) by U.S. person(s) owning at least 10% interest – (Category 2 filer)

3. Contribution of property by U.S. Person to a foreign partnership, after which (a) U.S. person owns at least 10% interest in such partnership or (b) the value of the property contributed (taking into account value of certain contributions made within prior 12-month period) exceeds $100,000 – (Category 3 filer) (note: additional separate Category 3 filing would be required if partnership later disposed of the contributed property while the U.S. person was still a partner)

4. Additional occasions when U.S. person acquires or ceases to hold a 10% interest in a foreign partnership – (Category 4 filer).

G. Interests in certain foreign disregarded entities ("FDEs") – IRS form 8858

An "FDE" is an entity that is organized under non-U.S. Law and that is disregarded as an entity separate from its owner for U.S. income tax purposes, including a non-U.S. entity that has elected under U.S. "check the box" regulations to be disregarded.

1. Legal ownership by a U.S. person of an FDE

2. U.S. person that is either a Category 4 or 5 filer of Form 5471 with respect to a foreign corporation that is the "tax owner" of an FDE

3. U.S. person that is either a Category 1 or 2 filer of Form 8865 with respect to a foreign partnership that is the "tax owner" of an FDE.

The "tax owner" is the person that is treated as owning the assets and liabilities of the FDE for U.S. income tax purposes.

H. Interests in or relationship to certain foreign trusts – IRS Form 3520

A "foreign trust" is any trust (whether established under U.S. or non-U.S. law) whereby (a) a non-U.S. court has primary supervision over the administration of the trust or (b) a non-U.S. person has authority to control a substantial decision about the trust.

1. U.S. person who is treated as an owner of a foreign grantor trust under sections 671 through 679 of the U.S. Internal Revenue Code (the "U.S. grantor trust rules") – IRS Form 3520

2. U.S. person who received or is deemed to receive a distribution from a foreign trust – IRS Form 3520

3. U.S. person who is the "responsible party" for reporting a "reportable event" that occurred with respect to a foreign trust during the tax year being reported – IRS Form 3520.

I. Foreign grantor trust having U.S. owner pursuant to the U.S. grantor trust rules – trustee of such trust must file IRS Form 3520a.

J. U.S. person who transfers or is deemed to transfer property to a foreign corporation – IRS Form 926.

K. U.S. person who receives certain gifts or inheritance from a non-U.S. person – IRS Form 3520.

L. U.S. person having certain beneficial interests in certain Canadian registered retirement plans – IRS form 8891.

M. Complete IRS Form W-9 (or provide equivalent information) to foreign financial institutions in which U.S. investor has accounts or holdings to facilitate completion of IRS Form 8966 or equivalent under any relevant FATCA-related intergovernmental agreement.

March 17, 2017

INTERNATIONAL ESTATE PLANNING FOR UNITED STATES CITIZENS

By Michael W. Galligan*,
Partner, Phillips Nizer LLP

In Consultation With: An International Group of Experts**

For decades, if not for almost a century, it was widely assumed that any U.S. citizen who owned property or who resided outside the United States should have a separate Will for each jurisdiction in which the U.S. citizen resided or owned property. This assumption made sense in an era when each national legal system operated in apparent sovereign separation from other countries, with full discretion whether to enforce the judgments of other nations' courts and full liberty to decline to enforce other nations' tax laws. But the landscape has changed, especially after the end of the Cold War in 1989 and the terrorist attacks of September 11, 2001. As the European Union encompasses more and more countries, the respect generally granted to the judicial judgments and decisions of other countries, especially within Europe continues to increase;[1] similar developments are afoot in Latin America.[2] Perhaps, even more importantly,

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[1] Commonly referred to as "the Brussels Regime," all members of the European Union are now subject to the Brussels I Regulation (officially the Council Regulation (EC) No 44/2001 of 22 December 2000) on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. The Brussels I Regulation follows and incorporates the provisions of the 1968 Brussels Convention and the 1988 Lugano Convention dealing with the same issues. The so-called "Brussels IV Regulation," which becomes effective in August of 2015, introduces a new regime for the choice of succession law in all countries of the European Union save England, Ireland and Denmark and offers new opportunities for U.S. citizens to elect to have the law of a U.S. jurisdiction apply to the succession of their property, to the extent they own property in Europe or to the extent their succession is otherwise subject to the jurisdiction of one or more of the participating countries of the European Union.

[2] Major initiatives include the Inter-American Convention On Extraterritorial Validity Of Judgments And Arbitral Awards (Montevideo, 1979) and the Inter-American Convention On Jurisdiction In The International Sphere For

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* Most of the material in this paper appeared originally in an article in the October 2009 edition of <u>Estate Planning</u> Magazine (Thomson Reuters).

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countries seem increasingly willing to bind themselves to mutual exchange information and even assist in enforcing each other's tax laws as well as participate in multilateral security initiatives for which "tax evasion" ranks almost equally with money-laundering and terrorism as an evil to be defeated.[3]

I. Why A Unified Estate Plan Is Necessary

Even before these recent changes in the international climate, there are – and always have been – good practical reasons to organize an international estate plan to ensure that all property of a U.S. citizen could pass, directly or indirectly, under one comprehensive Will or Will substitute. To rely, without good reason, on multiple Wills is to court disaster: one Will may accidentally revoke another; the proper formalities for each relevant jurisdictions may not be followed; lack of clarity about the situs of particular properties may leave it unclear as to which Will governs what property. Even practitioners who focus mainly on domestic planning advise their clients to hold property outside the state of their domicile through limited liability companies or revocable trusts. This basic piece of common sense does not cease to apply when one crosses the borders of the United States!

But even more important reasons exist for seeking to integrate an international estate plan than the dangers of faulty drafting and duplicative estate proceedings

1. <u>The Need to Be Able To Use Trusts</u>. The trust is the workhorse of U.S. estate planning Most applicable exclusion, marital deduction, and charitable deduction planning is unthinkable without trusts. Lifetime planning transfers such as QPRTS, GRATS and GRITS and sales to grantor trusts depend self-evidently on the law of trusts. But many of the most important countries in the world view trusts differently. Under German law, transfers to trusts under German Wills violate public policy, while transfers to non-German trusts under non-German instruments incur gift and inheritance tax at the highest marginal tax rates. Switzerland

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The Extraterritorial Validity Of Foreign Judgments" (La Paz, 1984) as well as, for the Mercosur countries (Argentina, Brazil, Paraguay and Uruguay), the "Protocol of Cooperation and Jurisdictional Assistance on Civil, Commercial, Labor and Administrative Matters" (Las Leñas, 1992).

[3] The "Forty Recommendations" of the Financial Task Force (established by the G-7 Summit in Paris in 1989) include "Measures To Be Taken by Financial Institutions and Non-Financial Businesses and Professions to Prevent Money Laundering and Terrorist Financing" and "Institutional and Other Measures Necessary in Systems for Combating Money Laundering and Terrorist Financing."

recognizes trusts but looks through the trust to the underlying grantor or beneficiary for income tax purposes. The trust is not an institution fully incorporated in the internal law of any country in continental Europe, save Liechtenstein, in none of these countries can transfers to a trust be credited toward the share that a surviving spouse and children are required to inherit from their deceased spouse or parent. Japan has trusts but trusts still do not satisfy mandatory inheritance requirements for surviving spouses and children. England, the birthplace of modern trusts, does not have mandatory inheritance in the tradition of the civil code; nonetheless, the tax treatment of transfers to trusts under the Finance Act of 2006 does not accord with U.S. tax concepts: for example, transfers of English property to a revocable trust may trigger an inheritance tax charge of twenty percent.

But the problems do not stop with the uncertain status of the trust throughout much of the world.

2. Discordance Between U.S. Law and Non-U.S. Law. Most countries in the world (including many common law countries as well as most civil and Sharia law countries) think very differently than the United States about inter-generational wealth transfers, inheritance, family and creditor protection, how wills are made and implemented. Here are some resulting areas of concern:

(a) Community Property. To prepare an estate plan, one must know the nature and extent of the property for which one is planning: under the law of China, South Africa and Taiwan, as well as most countries in continental Europe and virtually all countries in Latin America, spouses own property in "community" unless they have expressly adopted another marital property regime such as separation of property. This means that a married U.S. citizen client may not have as much property to dispose of as the client thought! Moreover, a married U.S. citizen from a non-community U.S. state who purchases a residence or a business in a community property country might effectively be making a gift of one-half of the property to the non-purchasing spouse at the time of the acquisition. This could create significant U.S. gift and estate tax issues if the non-purchasing spouse is not a U.S. citizen. Conversely, there may also be significant planning opportunities when the purchasing spouse is neither a U.S. citizen nor a U.S. domiciliary.

(b) Mandatory Inheritance. Virtually every country in Latin America, continental Europe, the Middle East (except Israel) and important countries in Asia (including Japan, Korea and Taiwan) require that spouses, descendants and sometimes parents inherit, or have a claim to, a portion of or interest in their decedent's property, regardless of what the decedent's will may provide; in countries where Sharia law applies, this requirement can even extend to siblings. These shares can apply to as much as three-fourths of a decedent's property. Furthermore, lifetime transfers must often be added back for purposes of determining the value of the putative "reserve" for division among mandatory heirs.[4] Sharia law, at least as applied in the United Arab Emirates, forbids a testator from leaving the "free" portion (one-third) of an estate to beneficiaries entitled to a share of the two-thirds mandatory portion. Mandatory or "forced" heirship rules perhaps have the greatest potential for playing havoc with a U.S. estate plan. Few circumstances can deal a more devastating blow to a typical plan for a U.S. married couple to defer estate taxes until the death of the surviving spouse than a provision of a non-U.S. jurisdiction that requires a non-U.S. citizen spouse or child (whether U.S. or not) to inherit large amounts of property outright upon the death of the first spouse to die.

In parallel fashion, most of the major common law countries such as England (only in the case of the English domiciliaries), Ireland, Canada, Australia and New Zealand- allow a Will to be reformed after a decedent's death to provide for the support of family members and care providers who can establish need for post-mortem support or an equitable share in a decedent's property, while China provides that family members who were supported by the decedent should share in the estate. While not as likely to ruin a proper U.S. estate plan as mandatory inheritance rules of "civilian" countries, the risks are still there.[5]

(c) Unlimited Liability. Under the law of Japan, Korea and Taiwan, as well as many countries in Europe and Latin America, heirs are deemed to inherit property from a deceased person immediately upon death, without a common law estate administration (thus the

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[4] In Switzerland, for example, transfers made in the five years prior to death and transfers made with an intent to deprive an heir of a reserve portion must be added back. Other countries have no necessary limit on the duration of the "look-back" period.

[5] That this article looks for ways to protect a U.S. citizen's estate plan from being defeated by mandatory inheritance rules or other pre-emptive inheritance provisions does not in any way imply that these inheritance rules are wrong as a matter of policy. Avoidance of the application of these rules, however, is generally required in order to construct an estate plan consistent with current U.S. property and tax concepts.

distinction between common law "probate" and civil law "succession") but the corollary is that heirs assume liability to creditors of their decedent even if the liabilities exceed the value of the inherited property. Usually, an election can be made to limit this liability to the value of the assets actually inherited, which then gives rise to something akin to a common law estate administration. But the time limits on making this election are often very short – one month in Switzerland, three months in Japan, Korea and Taiwan – and failure to make a timely decision is not easily repaired.[6]

(d) Conflicts of Laws. Wrapped around all of these issues is the challenge of knowing with reasonable certainty the law that will apply to a U.S. client's testamentary plan in the first place. Through the first half of August, 2015, the main options have been nationality with regard to all property (e.g., Austria, Germany, Italy, Japan, Poland, Spain, Sweden, Taiwan); residence with regard to all property (e.g., Argentina, Brazil, Denmark, Finland, Switzerland); domicile with regard to all property (e.g., Chile, United Arab Emirates[7]); situs for immoveable property and domicile/residence for moveables (e.g., Belgium, Canada, Costa Rica, France, Israel, Russia, South Africa); situs for real property and domicile for personal property (Australia, Canada, Ireland, New Zealand and the United Kingdom), situs for real property and shares of companies and domicile for other moveables (e.g., China and Ukraine), situs for real property and nationality for everything else (Monaco). Beginning in mid-August of 2015, all countries of the European Union other than England, Ireland and Denmark will make a decedent's habitual residence the principal criterion of what law governs a succession while allowing for a voluntary choice of the law by a testator of the law of the testator's law of nationality as an alternative. The diverse ways in which non-U.S. courts apply "foreign law" is a great source of uncertainty. Do they apply only the "substantive law" or the "whole law"? If the whole law, do they accept a referral back ("remission") to their own laws or a referral to ("transmission") the laws of a third country? To what extent will they entertain a "foreign court" or "double remission" approach? The next worse thing to the derailment of a U.S. estate plan by

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[6] China limits the liability of heirs to the assets of the succession but any renunciation of an inheritance governed by Chinese law – whether for U.S. tax planning or other reasons – must be exercised within only two months of the decedent's death.

[7] In the United Arab Emirates inheritance matters are subject to the jurisdiction of the religious (Sharia) courts, for whom civil and common law choice-of-law concepts are relatively novel, and which therefore, in practice, generally apply Sharia law across the board.

discordant non-U.S. property and inheritance rules is the derailment of the plan by a failure to correctly identify the proper law of the country that will apply to estate property or an unforeseeable change in the "private international law" of the country that has to make that decision.

(e) Inheritance Taxes. Many countries have inheritance taxes, sometimes with rates of tax that approach and in certain cases even exceed U.S. rates: Belgium, Chile, Dominican Republic, Finland, France, Germany, Greece, Ireland, Italy, Japan, Korea, Netherlands, Norway, Poland, South Africa, Taiwan, Ukraine, United Kingdom, and Venezuela. Canada and Peru each have income taxes that serve as an inheritance tax substitute. Some Brazilian states and Swiss cantons also impose inheritance tax. In most cases, these taxes would be applied on a worldwide basis if a U.S. citizen died a domiciliary or resident of the relevant jurisdiction. Interesting exceptions are Chile, which taxes non-Chilean property of a U.S. citizen resident in Chile if the non-Chilean property was acquired with Chilean source funds, and Taiwan, which taxes the non-Taiwanese property of a Taiwanese national. While having no Mexican inheritance tax, Mexican states have transfer taxes that would apply to transfers of real property by reason of death.

The estate tax credit for "foreign death taxes" under IRC Section 2014 covers "foreign" inheritance taxes imposed on "foreign" property. The rules for determining if property is "foreign" for credit purposes generally follow the IRC Section 2105 rules for determining if U.S. property owned by a non-U.S. person is exempt from U.S. estate tax because it is located outside of the United States. But reliance on the credit is not always satisfactory because the United States only credits taxes paid to the United States on the property taxed abroad while the country abroad may tax property eligible for the U.S. marital or charitable deductions. Moreover, the Section 2014 credit does not apply to "foreign" taxes on property located in the United States. Some relief for U.S. citizens or beneficiaries in this situation is provided by "modern" U.S. estate tax treaties with such countries as France, Germany, Netherlands and the United Kingdom and by the Income Tax Treaty with Canada. The "older" estate tax treaties with Finland, Greece, Ireland, Italy, Japan, South Africa and Switzerland may also afford protection depending on the circumstances. But there is no such treaty protection for

U.S. citizens who reside in such countries with significant worldwide inheritance taxes as Belgium, Chile, Korea, Philippines, Poland, Turkey, Ukraine and Venezuela.

II. How To Create A Unified Estate Plan

This article focuses on a strategy of converting a client's non-U.S. property into U.S. property by employing a U.S. entity – particularly a U.S. limited liability company – to hold all non-U.S. property owned by a U.S. citizen domiciled in the United States and, in some instances, all U.S. as well as non-U.S. property owned by a U.S. person domiciled abroad. The purpose is to unify a U.S. citizen's estate plan so that U.S. planning documents will govern all non-U.S. property and minimize as much as possible the ability of discordant non-U.S. property and tax rules to undermine the integrity of the U.S. estate plan. As discussed below, the first step in international planning for U.S. citizens should be to consider this "holding company" approach and then to supplement it with other measures to the extent that it cannot stand on its own.

1. Characteristics of the Limited Liability Company. A limited liability company has great legal and tax flexibility under U.S. law. From a tax perspective, a single-member LLC is completely disregarded for U.S. tax purposes (absent an election to be treated as a corporation) and, if there are two or more owners, treated as a partnership (in the absence of an election to be treated as a corporation). Thus, one can avoid the two-tiered system of taxation associated with C corporations and also the exclusion of the underlying assets from cost basis "step-up" at a shareholder's death, which, absent careful planning, may preclude underlying assets of an S corporation as well as assets of a C corporation from this important benefit. In the case of a multi-member LLC, the ability to make a basis "step up" election under IRC Section 754 also allows persons who inherit membership interests a measure of tax deferral with respect to sales of LLC assets after a decedent's death.

2. Effect of a Unified Plan: Results from International Estate Planning Survey. In preparation for this article, a survey was conducted among leading non-U.S. succession and tax law counsel in some of the most important countries with which U.S. citizens own property or live, including Argentina, Australia, Austria, Belgium, Brazil, Canada, Chile, China, Costa Rica, Denmark, Finland, France, Germany, Hong Kong, India, Ireland, Israel, Italy, Japan, Korea, Mexico, Monaco, Netherlands, New Zealand, Panama, Philippines, Poland, Russia, Singapore,

South Africa, Spain, Sweden, Switzerland, Taiwan, Ukraine, United Kingdom, and United Arab Emirates.[8] On the basis of this survey, it appears that effectively converting the non-U.S. assets of a U.S. citizen to U.S. assets by interposing a U.S. LLC between the U.S. citizen and the non-U.S. assets often reduces or even eliminates the applicability of non-U.S. property, succession and tax law principles that would interfere with the smooth application of the U.S. citizen's estate plan. When the use of a U.S. holding company does not afford complete protection from discordant non-U.S. inheritance and tax rules, the U.S. estate plan can still be protected by assuring that favorable non-U.S. choice of law principles are fully exploited, utilizing pre-mortem and post-mortem renunciations in the non-U.S. jurisdictions, having all heirs join in an inheritance or succession agreement enforceable in the United States, or carefully drafting the dispositions under the U.S. planning documents to encourage maximum cooperation by the heirs with the U.S. citizen's estate plan.

(a) Permissibility of Transfers of Non-U.S. Assets to U.S. LLC. Of the jurisdictions surveyed, Australia, Belgium, Brazil, Canada, Chile, Costa Rica, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, Korea, Mexico, Monaco, Netherlands, New Zealand, Panama, Russia, Spain, Sweden, the United Kingdom, Ukraine and the United Arab Emirates generally permit a home owned by a U.S. citizen to be transferred to a U.S. LLC. Transfers of a home in Australia require the approval of the Treasurer (easily granted); transfers of real property in areas near the borders of Argentina and Brazil require administrative approval; neither individuals nor non-Chilean entities can own real property near Chilean borders. In Costa Rica, the LLC would need to appoint a legal representative to act for and represent the LLC before the Costa Rican public registry and all other Costa Rican legislation related to real property must be duly followed. Administrative approval is also required for transfers of real property near Mexican borders or the Mexican coast, which must generally be held in the first instance by a Mexican trust or, if for commercial purposes, by a Mexican entity whose corporate parent can be a U.S. LLC. Transfers of homes in Austria require provincial approval, which are reviewed more intensively in the Alpine regions; Denmark imposes some restrictions on transfers to non-EU entities; transfers of homes in Korea require a report to a government bureau. In Poland, an official permit would be required, with evidence of

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[8] Copies of the survey, responses and related correspondence are on file at the offices of Phillips Nizer LLP.

the LLC's owner's ties to Poland. A U.S. LLC, like any other non-Philippine person, may effectively hold only an interest in a condominium, as long as Philippine persons own at least 60% of the property. To own real property in South Africa, a U.S. LLC must interpose a South African company. A U.S. LLC cannot generally own a home in China without establishing a representative office in China, a relatively easy hurdle to overcome; interposition of a Hong Kong or a Singapore company could also be considered. As to Singapore, the approval of the Minister of Law is required other than for apartments in buildings governed by specific Planning Act schemes. For Taiwan, the ability of a U.S. citizen to own non-agricultural real property—and, thus, the ability to transfer it to a U.S. LLC—depends on whether the U.S. citizen's home state permits Taiwan citizens to own property in that state (apparently the case in 43 states). Transfers of homes in Switzerland and India to a U.S. LLC are currently more difficult because of general limitations on foreign ownership of real estate.

All the surveyed countries permit transfers of tangible property owned by a U.S. citizen to a U.S. LLC, on condition that works of art are not "national patrimony" (Italy), "of historical significance" (Poland), subject to a state option to purchase unique works of art (Denmark). A U.S. LLC may own works of "cultural value" located in Russia or Ukraine but may not be able to move the works permanently outside of either country.

The great majority of the surveyed jurisdictions permit transfers of business interests owned by a U.S. citizen to a U.S. LLC. In Argentina, Brazil, Japan, Korea and Ukraine, a U.S. LLC owning a local company would have to register the U.S. ownership with local authorities and a government permit is often required in the case of Poland. If a U.S. citizen resides in South Africa, transfers of South African business interests would be subject to approval by the foreign exchange authority ("ExCon"). Transfers of shares of certain commercial and professional Monaco companies require government consent. While there are no express provisions of Russian law prohibiting non-Russian ownership of Russian business entities, the September 1999 legislation on foreign investment must be followed. Taiwan permits transfer of Taiwanese companies upon approval of a business plan by Taiwan's Investment Commission.

(b) Impact on Non-U.S. Community Property. Of the surveyed countries, each of Belgium, Brazil, Chile, China, Costa Rica, Denmark, France, Italy, Mexico, Netherlands, Philippines, Russia, South Africa, Spain, Sweden, Switzerland and Ukraine has some form of community property as its default regime for regulating property ownership by spouses.[9] However, in some countries such as Belgium, Sweden and Switzerland, local community property rules generally apply only when at least the U.S. citizen spouse and sometimes both spouses resided in the country at the time of marriage or when the property was acquired; in the Philippines, the rules do not apply if both spouses are non-Philippine citizens even if Philippine residents. In a number of countries, including Chile (real estate only), Italy, Russia, South Africa, Sweden (real estate only) and Taiwan, the consent of both spouses appears to be required to effect the transfer of community property to an LLC. Even with such consent, the community property regime may simply adhere to the U.S. LLC interests for which the non-U.S. property was exchanged, at least in community property states like California, New Mexico or Texas and states such as New York that have adopted the Uniform Community Property Rights at Death Act.

(c) Impact on Non-U.S. Inheritance Regimes. Of the surveyed countries, all but India, Israel and South Africa (in the latter two countries, save for an exception for spousal maintenance) have at least some rules regarding inheritance that are inconsistent with U.S. inheritance rules. Here, one must carefuly consider whether the U.S. citizen will be considered by a U.S. jurisdiction to be its domiciliary and whether any non-U.S. jurisdiction might consider the U.S. citizen to be its domiciliary or resident. One must also consider whether the non-U.S. property was first acquired by the U.S. citizen personally or by the LLC.

(i) Effectiveness of Transfers to U.S. LLC. A transfer to a U.S. LLC of property with a situs in a non-U.S. jurisdiction owned by a U.S. citizen considered by that same jurisdiction to be domiciled or resident in the United States appears to afford protection from the application of discordant inheritance rules in the following jurisdictions: Australia, Belgium, Brazil, China (excepting real property and business interests), Costa Rica, Denmark, France, Germany, Ireland (possibly excepting real property), England and Wales, Mexico,

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[9] In Costa Rica, community property rules only become effective upon the dissolution of a marriage or civil union.

Monaco, Netherlands, Panama, Poland (as long as the transfer is a sale and not a gift), Russia, Switzerland (except for real property), Taiwan and the United Arab Emirates.[10] In addition to the protection afforded in these countries, protection appears to be afforded by all of the countries just mentioned as well as in the following jurisdictions when the property is first acquired by the LLC rather than by the U.S. citizen: Canada, Finland, Ireland (for real property as well), Italy, Japan, Philippines, Poland and Sweden. As a practical matter, transfers of property to a U.S. LLC with a situs in other jurisdictions that have mandatory inheritance rules may still afford protection in these jurisdictions because judicial proceedings, which are not common in the administration of a succession, may be required to enforce these rules on property not owned in the decedent's own name.

In the case of a U.S. citizen domiciled or resident in a non-U.S. jurisdiction, the protection afforded by a U.S. LLC is often less, especially if the situs country applies the law of domicile or residence to the inheritance of intangible assets, because the inheritance of the U.S. citizen's LLC interest would then be governed by the law of the non-U.S. country where the U.S. citizen is considered most likely domiciled or resident. But here, local "private international law" may help. Switzerland allows a non-Swiss national, even if a Swiss resident, to elect to have national law apply to Swiss as well as non-Swiss property.[11] Each of Poland, Spain and Sweden applies nationality law to its residents but does not necessarily apply its own law even when nationality law would defer to the law of residency (technically, "accept remission or '*renvoi*'"), so that U.S. law could still apply to all property of a Spanish or Swedish national, even Spanish or Swedish real property.[12] In the case of Italy, which follows the nationality principle but accepts remission, a U.S. citizen may be able to achieve the same result by directing in his or her Will that remission should not apply.[13] Transfer of Brazilian property owned by a U.S. citizen residing in Brazil to a U.S. LLC would cause Brazilian rules not to apply to it.

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[10] As noted above, jurisdiction over inheritance, in the UAE, is lodged in the Sharia courts and these courts may be more easily persuaded to ignore the formal rules of UAE "secular" law.

[11] Belgium has a similar rule as long the law of nationality cannot deprive an heir of a reserved portion.

[12] For a helpful discussion of the relevant Spanish case law, see David Hayton, *European Succession Law* (London) at 456-457.

[13] See, Article 13, Law of May 31, 1995, No. 218, discussed by Hayton, at 331-332. This should be the case where the relevant U.S. jurisdiction would not accept remission ("*renvoi*") or would otherwise honor such a provision.

(ii) Supplemental Measures. In cases where a transfer of local assets to a U.S. LLC does not completely exempt the property from local inheritance rules, the transfer may help accomplish the desired result. In some jurisdictions, transfers of "reserve" property to a U.S. LLC would be voidable but not void. In many jurisdictions, an heir who claims to be disadvantaged by a pre-mortem transfer must take affirmative steps to assert claims against transfered property in the courts of that jurisdiction. In Argentina, for example, a court may consider such circumstances as whether the transfer to the LLC was for adequate and full consideration; when the assets were directly acquired by the LLC, an Argentine court is less likely to set aside the transfer. In some jurisdictions, a court may also take into account the degree to which, as a practical matter, the disposition of the assets of the LLC in a U.S. citizen's testamentary plan are as generous to an heir as the enforcement of a mandatory heirship share would be.

When a transfer of non-U.S. assets to a U.S. LLC does not afford unquestionable protection from local inheritance rules, a second and even a third "line of defense should be applied," such as an agreement by the beneficiaries of the US estate, as a condition to their inheriting under the U.S. plan, not to challenge any of the transfers to the U.S. LLC, to require that the transfers be added back in any local "reserve" calculation and to sign any local instruments of renunciation that may be necessary to fulfill this purpose.[14] Most countries surveyed have provisions for post-mortem renunciation of statutory shares and several countries—Austria, Denmark, Finland, Germany, Poland, Sweden, Switzerland and Taiwan—even allow for pre-mortem renunciations of forced or mandatory inheritance shares.[15]

An even stronger line of defense would be to include an *in terrorem* clause in the U.S. Will that would disinherit any beneficiary who chose to try to enforce rights under non-U.S. law that violate the estate plan. An alternative, especially in states that disfavor *in terrorem* clauses, would be to condition legacies under a U.S. Will, whether outright

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[14] A renunciation of forced heirship rights generally serves a different purpose than a "qualified disclaimer" under U.S. tax concepts. Presumably, in most instances, the consideration for renouncing a forced heirship right - usually asset protection and the discharge of moral as well as legal obligations to family members - will satisfy the IRC requirement of "full and adequate consideration" to avoid any U.S. gift tax liability.

[15] Russia only allows for renunciation of property inherited through the non-compulsory or "free" share and beneficiaries of a renunciation must generally be those eligible for mandatory shares from the renouncing party.

or in trust, on cooperation in the post-mortem implementation of the U.S. plan. Such conditions should be enforceable in any U.S. jurisdiction (except possibly Louisiana) on the basis that a beneficiary would have no legal right to compel a legacy from the decedent and therefore the decedent can impose any condition that does not violate public policy. Conditional bequests are not generally contrary to public policy in the United States and it is U.S. courts to which estate fiduciaries as well as beneficiaries of a U.S. citizen would be looking to enforce the terms of U.S. planning documents.

(d) Impact on Unlimited Liability. Of the surveyed countries, the following provide that persons who inherit property from a decedent generally inherit unlimited personal liability for their decedent's unsatisfied debts: Argentina, Austria, Belgium, Chile, France, Germany, Italy, Japan, Korea, Netherlands, Poland, Spain, Switzerland and Taiwan. Some countries—including Belgium, Germany, Italy, Spain, Switzerland and Taiwan—do not apply this principle if, under their choice of law rules, their own law does not apply to a decedent's succession. Thus, the efficacy of a transfer of assets in any of these jurisdictions to a U.S. LLC would depend on the extent to which such a transfer would protect the assets from the reach of the inheritance rules of that jurisdiction.

(e) Impact on Inheritance Taxes. Of the surveyed countries, the following impose meaningful inheritance or inheritance-related taxes: Belgium (regional), Brazil (state level), Canada (deemed capital gains tax), Chile, Denmark, Finland, France, Germany, Ireland, Italy, Japan, Korea, Monaco (not on transfers to spouses, descendants and ascendants), Netherlands, Philippines ("estate tax"), Poland, South Africa, Spain, Switzerland (cantonal, with total exemption for spouses and exemptions or low rates for descendants), Taiwan, Ukraine and United Kingdom.

(i) U.S. Citizen "Domiciled" or "Resident" in the United States. It appears that transfers by a U.S. citizen of assets located in the following jurisdictions to a U.S. LLC should cause the assets not to be subject to that jurisdiction's inheritance taxes, at least if the US citizen is not considered by that jurisdiction to be its domiciliary or resident (or, in the case of Taiwan, a national): Belgium, Brazil (unless an heir is a Brazilian resident or the transferred assets are mainly real estate), Canada, Chile, Denmark, Finland (unless heir is a

Finnish resident or asset is Finnish real estate or Finnish real estate company interests), France (only for moveable assets), Germany (as long as the LLC qualifies as a corporation for German tax purposes and an heir is not a German resident), Ireland (as long as an heir is not an Irish resident), Italy (if interests in the LLC are not solely owned by the decedent), Japan (unless an heir is a Japanese resident), Korea (but subject to a “clawback” for some transfers made within the previous five years), Monaco, Netherlands (as long as the assets of the LLC do not consist principally of Netherlands real property), Philippines, Poland, South Africa, Spain (in certain cases for immoveable assets only as long as an heir is not a Spanish resident), Taiwan, Ukraine (as long as an heir is not a Ukrainian resident) and the United Kingdom. The same exclusion appears to apply to local real property transfer taxes on the inheritance of Mexican real property As explained above, the U.S. estate credit under IRC Section 2014 may be useless if there is no U.S. tax against which to apply the non-U.S. tax payment. When there is a U.S. tax, the effective non-U.S. tax rate on the non-U.S. property may be higher than the effective U.S. rate. By removing the property from taxation in the non-U.S. country, one may be able to avoid the non-U.S. tax entirely.

(ii) <u>U.S. Citizen Residing Abroad</u>. The estate of a U.S. citizen residing in one of the above-mentioned countries could be subject to inheritance tax on all property, including U.S. property. A beneficiary of that U.S. citizen who resides in one of these countries other than Brazil could be subject to inheritance tax on inherited U.S. property as well as inherited property located in that country. As mentioned above, the Section 2014 credit does not cover non-U.S. taxes on U.S. property and the United States does not have estate tax treaties with many countries, including, of the surveyed countries that tax inheritances, Belgium, Chile, Denmark, Korea, Philippines, and Ukraine. Denmark, Chile, Korea and the Philippines have their own foreign death tax credit, each of which measures appears to effectively provide a credit against local tax for the U.S. estate tax on U.S. property. Belgium gives a credit for non-Belgian taxes on non-Belgian real property. For countries like the Ukraine, in order to claim the benefit of the Section 2014 credit for non-U.S. inheritance/estate taxes on U.S. property, one may have to consider placing the U.S. assets in a special holding company organized under the laws of the country where a U.S. citizen resides in order to convert the U.S. assets in to non-U.S.

assets eligible for the credit.[16] The special holding company could still be owned by the U.S. LLC at least as long as the U.S. citizen is the only member of the LLC, thus preserving the unity of the estate plan, and the jurisdiction of a U.S. court over the administration of all estate assets.

3. Income Tax Issues. As mentioned earlier, a decision to adopt a strategy of organizing all non-U.S. assets of a U.S. citizen to a U.S. LLC can only be made after taking into account all U.S. as well as non-U.S. tax consequences of the transfers and the tax treatment of the U.S. LLC once the transfers have been completed. From a U.S. tax point of view, the U.S. LLC would be disregarded as long as the U.S. citizen is the sole owner or as a partnership if there are two or more owners, absent a check-the-box election to the contrary. Among the surveyed countries, the LLC would or could be treated as a pass-through entity in France and Switzerland, much as in the United States. Germany looks to several different factors to determine if an entity should be taxed as a corporation or as a partnership. The limited liability feature of the LLC makes it more likely to be treated as a corporation but placing a limit on the duration of the LLC might help to avoid that result.[17] Similar considerations may apply for Austria and Korea.

(a) When LLC Is Treated as Corporation under Non-U.S. Tax Rules. In the following countries, it appears the LLC would be taxed as (or like) a permanent establishment at corporate tax rates: Argentina (for income from Argentine real estate), Australia, Austria (for income from Austrian real estate), Belgium, Brazil, Canada, Costa Rica, Denmark, France, Germany, Netherlands, Ireland, Israel, Japan, Russia, South Africa (with respect to South African business interests), Spain (depending on nature of activities in Spain), Sweden, Ukraine and the United Kingdom. In the case of a solely-owned LLC classified as a corporation by the non-U.S. jurisdiction, the United States disregards the foreign characterization of the LLC as much as it does its US status as a separate legal entity. As a result, the taxes paid by the LLC to the non-U.S. jurisdictions should be treated as paid by the U.S. citizen owner and therefore fully creditable against the U.S. citizen's taxes on the same income. If the LLC had more than one

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[16] Under Article 25 of the Ukraine Income Tax Treaty, which governs all types of taxes, Ukraine should not impose higher inheritance taxes on a U.S. person holding Ukrainian property than it does on a Ukrainian person.

[17] To avoid the application of Germany's forced heirship rules, however, it is advisable for the LLC to be treated as a corporation.

member, the non-U.S. taxes should be similarly allocated to the LLC members for credit purposes.

However, other issues need to be considered. For example, if a country taxes the U.S. LLC at a higher rate of taxation than that to which a U.S. citizen or the members of an LLC is subject, there could be an additional cost. Corporate rates of tax in most of the surveyed countries do not exceed 35% but withholding or similar taxes on dividends and distributions imposed by jurisdictions such as Germany, South Africa and Spain could push the effective tax rate above U.S. rates, unless, as is the case with Chile, the corporate tax is credited against the withholding tax. Excess foreign tax should not be creditable against U.S. income tax unless the U.S. citizen has other non-U.S. source income that is taxed at a lower rate than the U.S. tax in the same year or an eligible carry-over year.[18] The imposition of a VAT tax by a jurisdiction such as the Ukraine could also push the effective tax rate above 35% and, in any event, VAT tax is not generally creditable for U.S. income tax purposes.

(c) <u>Coping with Possible Non-U.S. Capital Gains Taxes</u>. Some countries may impose a capital gains tax on the transfer to a U.S. LLC of real property that the U.S. citizen acquired in his or her own name before transferring the assets to the LLC. These include Argentina (nominal rate of 1.5%), Australia (but not if U.S. citizen is only shareholder), Canada (if the LLC is treated as a corporation), China, Denmark (except for a home), Finland, France, Germany, Ireland, Japan, Philippines, Poland, Russia, South Africa, Spain, Sweden, Switzerland (cantonal) and Taiwan.[19] A transfer of real property in Italy or Monaco would incur various registration or transfer taxes and duties but no gains tax. A transfer of Spanish real property would be subject to transfer and stamp duties of 7%. A transfer of Brazilian real property would incur a transfer tax of 2% to 6% but no capital gains tax as long as the property transferred to the LLC is capitalized at cost rather than market value. Netherlands imposes 6% transfer tax and

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[18] Note that some countries, such as Belgium, Germany, Ireland and the United Kingdom (when the owner is a U.K. resident) may tax rent-free use of a home owned by a U.S. LLC that is treated as a corporation on an imputed income basis.

[19] The mention of France and Italy in this sentence prescinds from the argument suggested in Part II(3)(a) above (especially material to which Footnote 17 is attached) that, under the recent Protocol to the United States-France Income Tax Treaty and the recent United States-Spain Competent Authority Agreement, taxing a transfer by a U.S. resident of an interest in French or Spanish real property to a U.S. LLC should not give rise to French or Spanish capital gains tax because such a tax would be inconsistent with the "pass-through" nature of the U.S. LLC under U.S. tax law.

Singapore and Hong Kong impose stamp duties of up to 3% and 3.75% respectively. It cannot be emphasized too much that in virtually all these instances no such capital gains or transfer taxes would be imposed if the non-U.S. real property were purchased directly by the LLC. The transfer of business assets of some countries to a U.S. LLC may also incur gains or transfer taxes, including interests in Canada, Denmark, Philippines and Sweden. Again, initial acquisition of such non-U.S. business interests by the U.S. LLC would avoid these taxes. Contribution of retail or industrial real property in Mexico, assuming no capital gains tax is incurred by virtue of the United States-Mexico Competent Authority Agreement, may still give rise to a 15% value added tax, which, with proper planning, may be eligible for a subsequent Mexican credit or refund.

If one is dealing with a jurisdiction with which the United States does not have an income tax treaty or the relevant treaty does not adequately address the tax treatment of pass-through entities owned by U.S. persons, a transfer of non-U.S. assets to a U.S. LLC by a U.S. citizen may trigger a non-U.S. gains tax that will not be an event of recognition for U.S. income tax purposes and, therefore, no U.S. income tax credit for the foreign tax would be currently available. In that event, one could consider having the U.S. LLC form a wholly-owned subsidiary in the non-U.S. country. Since the LLC is a disregarded or pass-through entity, the contribution of the non-U.S. assets to the non-U.S. subsidiary would trigger U.S. capital gains tax against which the capital gains tax paid to the non-U.S. country could be claimed as an income tax credit. The cost basis for gains tax purposes would have been "stepped up" in both countries to the value on the date of the transfer. Once the transfer was complete, the U.S. citizen or LLC could make an election to have the subsidiary treated for U.S. income tax purposes as a partnership and any subsequent sale of the property could then be taxed in both countries at the same time with a parallel increase in basis and a U.S. credit for the tax paid to the other country.[20]

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[20] I wish to acknowledge the contribution of my partner, Tiberio ("Tibi") Schwartz, to the thinking reflected in this paragraph. In some cases, payment of the non-U.S. gains tax when no U.S. credit is available may still be tax efficient where a non-U.S. country has no special exemption for U.S. capital gains tax on real property passing at death and no "step-up" in cost basis. The U.S. citizen would be effectively pre-paying the non-U.S. gains tax that heirs would have to pay upon a sale of the property after the U.S. citizen's death, with funds that would otherwise be subject to U.S. estate tax on the U.S. citizen's death.

4. Alternative Holding Entities. If it is determined that using a wholly owned U.S. LLC as a holding entity would have adverse capital gains tax or other tax consequences, serious inquiry should be made about the utility of a partnership, including a limited partnership as a holding entity, to accomplish the unitary estate planning objectives for which this article advocates. The use of partnership to accomplish this result appears to have some promise in Austria, Ireland and the United Kingdom and may, with appropriate adjustments, work in other jurisdictions as well.

For property located in a common law jurisdiction, the trust may be another alternative, but, at least in the United Kingdom, there may be a mismatch between the U.S. and U.K. tax rules even more serious than with an LLC. The status of trusts in China, Japan and Korea deserve monitoring. A U.S. trust might be able to act as an owner of property in civil law jurisdictions that have ratified or are expected to ratify the Hague Convention on the Recognition of Trusts (Italy, Luxemburg, Monaco, Netherlands and Switzerland) as well as countries such as Austria, Belgium and France, which, in their internal law, now recognize trusts organized in common law countries as having legal status.

III. Final Word - When More Than One Will Must Be Used

In some cases, organizing the disposition of all the non-U.S. assets of a U.S. citizen under one Will or as part of a U.S. holding entity may not be feasible. Take real property in Italy: heirs of Italian real property are exempt from Italian capital gains tax on the sale of the property.[21] If the heirs are U.S. persons, there will be no U.S. gains tax on pre-mortem appreciation. Transferring the Italian real property to a U.S. LLC might jeopardize the Italian gains tax exclusion. In this case, the U.S. Will could still direct the disposition of the Italian property, even if Italian court proceedings would be required to enforce the Will. As already noted, Italy is one of the few "civilian" countries that have ratified the Hague Convention on the Recognition of Trusts, transfer of Italian real property to a testamentary trust under a U.S. Will

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[21] Israel has a similar exemption for the sale of inheritance on Israeli real property interests used as a residence.

may be feasible if the U.S. Will directs that U.S. law should apply and that Italy should not "accept remission."[22]

In the event recognition of the U.S. will in a non-U.S. jurisdiction would be difficult or a non-U.S. jurisdiction would apply its own law and thereby endanger the dispositions under a U.S. will, the measures identified above "as second lines of defense" such as inheritance agreements, non-U.S. inheritance renunciations, in terrorem clauses and conditional bequests must play a primary role, even if resort to a non-U.S. will must be made. Great care must be taken to ensure that any non-U.S. will is properly coordinated with the U.S. will. U.S. clients need to clearly understand that U.S. counsel must be consulted when any property is acquired abroad and when any non-U.S. testamentary instruments are executed. As emphasized above, the effectiveness of a U.S. holding company strategy is often greater when the U.S. entity has made the initial acquisition of non-U.S. property and, in such cases, resort to a non-U.S. will should not be necessary. But, whatever the circumstances, any acquisition of non-U.S. property and any execution of a non-U.S. will must always invite review of the U.S. will and revision and re-execution of the U.S. estate planning documents after the non-U.S. transactions are complete.

\- March, 2015

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[22] See Section II (c)(i) and footnote 12 above.